STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Wisconsin Energy Corporation, Integrys Energy Group, Inc., Peoples Energy, LLC, The Peoples Gas Light and Coke Company, North Shore Gas Company, ATC Management Inc., and American Transmission Company LLC	)	
Application pursuant to Section 7-204 of the Public Utilities Act for authority to engage in a Reorganization, to enter into an agreement with affiliated interests pursuant to Section 7-101, and for such other approvals as may be required under the Public Utilities Act to effectuate the Reorganization.	)	Docket No. 14-0496

POSITION STATEMENT AND DRAFT CONCLUSIONS
OF
THE PEOPLE OF THE STATE OF ILLINOIS

The People of the State of Illinois

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TABLE OF CONTENTS

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I. Section 7-204 In General and the Appropriate Statutory Interpretation

A. AG's Position

Section 7-204(b) of the Public Utilities Act (the "Act") provides that no reorganization shall take place without prior Commission approval. 220 ILCS 5/7-204(b). Before approving any proposed reorganization, the Commission must find that:

> (1) the proposed reorganization will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service;
> (2) the proposed reorganization will not result in the unjustified subsidization of non-utility activities by the utility or its customers;
> (3) costs and facilities are fairly and reasonably allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by the utility for ratemaking purposes;
> (4) the proposed reorganization will not significantly impair the utility's

> ability to raise necessary capital on reasonable terms or to maintain a reasonable capital structure;
> (5) the utility will remain subject to all applicable laws, regulations, rules, decisions and policies governing the regulation of Illinois public utilities;
> (6) the proposed reorganization is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction;
> (7) the proposed reorganization is not likely to result in any adverse rate impacts on retail customers.

220 ILCS 5/7-204(b). In addition, Section 7-204(c) provides that the Commission "shall not approve a reorganization without ruling on: (i) the allocation of any savings resulting from the proposed reorganization; and (ii) whether the companies should be allowed to recover any costs incurred in accomplishing the proposed reorganization and, if so, the amount of costs eligible for recovery and how the costs will be allocated." 220 ILCS 5/7-204(c). The burden of proof is on the JA to demonstrate that these provisions have been satisfied.

Finally, the AG notes, and of particular importance to Peoples Gas and North Shore ratepayers, subsection (f) provides that "[i]n approving any proposed reorganization pursuant to this Section the Commission may impose such terms, conditions or requirements as, in its judgment, are necessary to protect the interests of the public utility and its customers." 220 ILCS 5/7-204(f).

The AG argues that the Joint Applicants' interpretation of Section 7-204 is unlawfully narrow and should be rejected. The AG pointed to the JA's statement in their Initial Brief that the Commission should reject the additional conditions sought by the AG and City/CUB "because they are not related to any of the findings required under Section 7-204." JA IB at 31. The AG asserted that JA's position is unlawfully narrow and should be rejected.

According to the AG, the argument betrays a fundamental misunderstanding of the requirements of Section 7-204, and the Commission's obligations under the entire statute.

Section 7-204(b) outlines the minimum service, safety and rate impact requirements that the Commission must conclude have been satisfied before approving a merger. 220 ILCS 5/7-204(b)(1)-(7). But in addition to Section 7-204(b), Section 7-204(f) creates a further obligation on the Commission to protect the public interest – not one that must be tied to the subsection 7-204(b) requirements.

The AG adds that in ascertaining the legislature's intent, courts begin by examining the language of the statute, reading the statute as a whole, and construing it so that no word or phrase is rendered meaningless or superfluous. *Kraft, Inc. v. Edgar*, 138 Ill.2d 178, 189, 149 Ill.Dec. 286, 561 N.E.2d 656 (1990); *Wal–Mart Stores, Inc. v. Industrial Comm'n*, 324 Ill.App.3d 961, 965, 258 Ill.Dec. 17, 755 N.E.2d 98 (2001). Illinois courts cannot view words or phrases in isolation but, rather, must consider them in light of other relevant provisions of the statute. *In re E.B.,* 2008 WL 4943447 Ill., 2008. The AG concludes that these statutory interpretation precepts require rejection of the JA's flawed statutory analysis.

The AG states that while it is true that Section 7-204(f) conditions, in effect, can be used to help ensure that the Section 7-204(b)(1)-(7) requirements are, in fact, satisfied post-merger, Section 7-204(f) also provides the Commission with an obligation to impose conditions that it believes are necessary and appropriate to protect the public interest. Adoption of the JA's restricted interpretation of Section 7-204 would, contrary to accepted statutory interpretation principles, render this subsection meaningless.

The AG notes that prior Commission orders related to proposed utility mergers support its position. For example, the AG pointed out that the Commission applied a condition designed to improve service quality in its 1999 order approving the merger between Ameritech, Inc. and SBC Communications, Inc., the acquiring, Texas-based corporation. In that decision, the

Commission imposed a condition that it specifically noted was necessary to *improve Americtech's existing service quality found to be deficient by the Commission* – not unlike the clear evidence in this case of mismanagement by Peoples Gas of its AMRP, and the requested AG/CUB/City conditions designed to set the AMRP operation on a better operational course. In the Ameritech/SBC case, the Commission ruled:

> *Ameritech Illinois' repeated failure to meet the OOS>24 service standard, however, suggests that the existing service quality mechanism in the Alternative Regulation Plan does not provide an adequate incentive for the company to comply with the standard.*
>
> […] *The Commission finds that imposing a condition that relates to Ameritech Illinois' avoided cost of meeting its service quality obligations should eliminate the company's current cost incentive not to meet the OOS>24 standard.* Accordingly, and pursuant to its authority under § 7-204(f), the Commission requires the Joint Applicants to demonstrate to the Commission, within six (6) months after obtaining all necessary regulatory approvals and closing the merger, that Ameritech Illinois is in compliance with the OOS>24 service standard. The Joint Applicants shall demonstrate compliance in the same manner currently used by the Commission and Ameritech Illinois to measure the company's compliance with the OOS>24 service standard. If, after notice and hearing, the Commission determines that the Joint Applicants have not demonstrated that Ameritech Illinois is in compliance with the OOS>24 service standard during the last month of the six month period, the Commission shall assess a $15 million penalty fine ($30 million X 50%), separate and apart from any annual rate reduction resulting from the service quality component of the company's Alternative Regulation Plan… […]
>
> *The condition the Commission imposes here is designed to ensure that the Joint Applicants focus on the OOS>24 problem and devote the necessary resources to meeting the standard.* The Commission has attempted to craft a condition that equates Ameritech Illinois' estimated costs of complying with the OOS>24 standard with the company's costs in avoiding it. The Commission believes that the condition is fair, protects Ameritech Illinois and its customers from risks resulting from the merger, and provides the necessary incentive to comply with the OOS>24 standard. (cites omitted)

In re SBC Communications, Inc. 1999WL 1331303 (ICC Docket No. 98-0555, September 23, 1999) (emphasis added).

The AG contends that this merger condition in the Ameritech/SBC case demonstrates that the Commission has authority under Section 7-204(f) to premise merger approval on the conditions it believes are necessary to protect the public interest, including conditions that would create *improvements in existing service.* It also aligns with the AG/City/CUB contentions that should the Commission approve the merger here, additional conditions are needed to improve the existing deficient management of the PGL AMRP. In other words, the AG claims that even if the JA had satisfied the requirements of Section 7-204(b) designed to ensure that the quality, reliability and cost of utility service is not negatively impacted, the Commission has an obligation to attach any additional conditions that "in its judgment, are necessary to protect the interests of the public utility and its customers." 220 ILCS 5/7-204(f). The AG concludes that the imposition of commitments that will help protect customer interests – interests that WEC has made clear are not its priority – is unquestionably appropriate and consistent with the Commission's obligations under the Act.

B. Commission Analysis and Conclusion Regarding the Proper Interpretation of Section 7-204 In General

The Commission agrees with the AG that the Joint Applicants' interpretation of Section 7-204 is unlawfully narrow. As the AG argues, well-settled rules of statutory interpretation require that statutes be read as a whole, and construed so that no word or phrase is rendered meaningless or superfluous. *Kraft, Inc. v. Edgar*, 138 Ill.2d 178, 189, 149 Ill.Dec. 286, 561 N.E.2d 656 (1990); *Wal–Mart Stores, Inc. v. Industrial Comm'n*, 324 Ill.App.3d 961, 965, 258 Ill.Dec. 17, 755 N.E.2d 98 (2001). Illinois courts cannot view words or phrases in isolation but, rather, must consider them in light of other relevant provisions of the statute. *In re E.B.,* 2008 WL 4943447 Ill., 2008.

While Section 7-204(f) conditions, in effect, can be used to help ensure that the Section 7-204(b)(1)-(7) requirements are, in fact, satisfied post-merger, Section 7-204(f) also provides the Commission with an obligation to impose conditions that it believes are necessary and appropriate to protect the public interest. The JA's interpretation of the statute's requirements reads out that portion of Section7-204 and, therefore, is contrary to accepted statutory interpretation principles.

The Commission also agrees with the AG's argument that the Commission has authority pursuant to Section 7-204 (f) to impose conditions that are designed to improve utility service. In our 1999 order approving the merger between Ameritech, Inc. and SBC Communications, Inc., the acquiring, Texas-based corporation, the Commission imposed a condition that it specifically noted was necessary to *improve Americtech's existing service quality found to be deficient by the Commission*. In the Ameritech/SBC case, the Commission ruled:

> *Ameritech Illinois' repeated failure to meet the OOS>24 service standard, however, suggests that the existing service quality mechanism in the Alternative Regulation Plan does not provide an adequate incentive for the company to comply with the standard.*
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> […] *The Commission finds that imposing a condition that relates to Ameritech Illinois' avoided cost of meeting its service quality obligations should eliminate the company's current cost incentive not to meet the OOS>24 standard.* Accordingly, and pursuant to its authority under § 7-204(f), the Commission requires the Joint Applicants to demonstrate to the Commission, within six (6) months after obtaining all necessary regulatory approvals and closing the merger, that Ameritech Illinois is in compliance with the OOS>24 service standard. The Joint Applicants shall demonstrate compliance in the same manner currently used by the Commission and Ameritech Illinois to measure the company's compliance with the OOS>24 service standard. If, after notice and hearing, the Commission determines that the Joint Applicants have

> not demonstrated that Ameritech Illinois is in compliance with the OOS>24 service standard during the last month of the six month period, the Commission shall assess a $15 million penalty fine ($30 million X 50%), separate and apart from any annual rate reduction resulting from the service quality component of the company's Alternative Regulation Plan… […]
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> *The condition the Commission imposes here is designed to ensure that the Joint Applicants focus on the OOS>24 problem and devote the necessary resources to meeting the standard.* The Commission has attempted to craft a condition that equates Ameritech Illinois' estimated costs of complying with the OOS>24 standard with the company's costs in avoiding it. The Commission believes that the condition is fair, protects Ameritech Illinois and its customers from risks resulting from the merger, and provides the necessary incentive to comply with the OOS>24 standard. (cites omitted)

In re SBC Communications, Inc. 1999WL 1331303 (ICC Docket No. 98-0555, September 23, 1999) (emphasis added).

The Commission's Order in the Ameritech/SBC case is consistent with the evidence in this case, where it is clear that if the Commission approves the transaction, additional conditions are needed to improve the existing deficient management of the PGL AMRP. In other words, even if the JA had satisfied the requirements of Section 7-204(b) designed to ensure that the quality, reliability and cost of utility service is not negatively impacted, the Commission has an obligation to attach any additional conditions that "in its judgment, are necessary to protect the interests of the public utility and its customers." 220 ILCS 5/7-204(f).

II. The Proposed Reorganization Violates The Requirement of Section 7-204(b)(1) to Not Diminish the Utility's Ability to Provide Adequate, Reliable, Efficient, Safe, and Least-Cost Service.

A. AG's Position

1. The Record is Clear that the Joint Applicants Failed to Demonstrate that They Are Ready, Willing, and Able to Assume Control of the AMRP.

The AG argues that the evidence shows that the Joint Applicants do not meet the requirements of Section 7-204(b)(1) because they did not meaningfully engage with the myriad problems with Peoples Gas's multi-billion dollar main replacement program. The AG asserts that the JA tried to marginalize, if not ignore altogether, the significance of the AMRP in this proceeding. Indeed, in its Initial Brief, the JA argued that the ongoing travails and the future of the AMRP are not relevant to this proceeding. See, *e.g.*, JA IB at 2, 33, 33-34. The AG states that despite JA's efforts, the AMRP emerged as a as the central issue for evaluating whether the merger should be approved under Section 7-204 of the Act.

The AG states the AMRP has been beset by poor management since the Commission approved the program in Peoples Gas's 2009 Rate Case. The first indication of the extent of the problems with Peoples Gas's project management was identified in the utility's 2012 rate case. In its Final Order in that case, the Commission found that the AMRP was besieged with troubles, stating:

> Part of the problem with the AMRP is the lack of detail. Staff examined Peoples' submissions to Staff DR ENG 2.12, which asked for a detailed explanation of its five-year plan for the AMRP, including all costs. They found: "There is no discussion of costs in the White Paper. There is no discussion of resource requirements or project management. The response to Staff DR ENG 2.12 states that the AMRP budget for 2013 is $220.75 million, but does not explain how Peoples arrived at that number and Attachment 01, the White Paper, does not address the issue either." *Id.* at 19. Additionally, Peoples also stated that they "have not determined the funding level past the year 2013". *Id.* Attachment 20.02.

2012 Rate Case Order at 61. The Commission was so concerned about the poor state of the program, it ordered "a two-phase investigation of the AMRP [be conducted] under Section 8-102 of the Act (220 ILCS 5/8-102) ending in a public document report." *Id.* Liberty's AMRP audit (and the Interim Report filed in January, 2015) are the result of the Commission's 2012 Rate Case Order.

The AG asserts that in the instant case AG witness Coppola and City/CUB witness Cheaks described an AMRP program that has not improved since the Commission's findings in its 2012 Rate Case Order. Among other problems, Mr. Coppola testified that a 2012 internal review of Peoples Gas's AMRP project management conducted by PWC "identified several deficiencies and 23 areas where improvements needed to be made." AG Ex. 2.0 at 16-17:341-342. Mr. Coppola pointed out that "as of October 2014, two years later, none of these improvements have been completed." *Id.* at 17:342-343. Mr. Coppola added that Peoples Gas and Integrys admit that they "have not formally defined a future state operating model or project delivery strategy in conjunction with the Rider QIP, or developed associated processes and controls." *Id.* at 17:350-353; AG Ex. 2.2. Mr. Coppola concluded that

> The scale of the AMRP seems to have overwhelmed the utility's resources. It has not proved itself capable of managing an accelerated main replacement program that is more than double in scope from what PGL was managing historically. The demands on the City of Chicago to respond to the increased activity of the AMRP also have taxed the resources of the City. The result has been huge cost overruns, delays in completing projects, and, in my view, a state of mass confusion and uncertainty as to whether or not the critical objectives of increasing safety, system reliability, operating cost reductions, and financial benefits to customers have actually been, or are likely to be accomplished.

AG Ex. 2.0 at 20:410-418.

According to the AG, City/CUB witness William Cheaks, Jr. identified some of the same issues with the AMRP raised by Mr. Coppola. For instance, Mr. Cheaks testified that although the 2012 PWC audit identified numerous serious deficiencies with the AMRP, Peoples

Gas "did not implement these measures, if at all, until August of 2014." City/CUB Ex. 3.0 at 6:102-103. Mr. Cheaks also added that Peoples Gas's coordination efforts with the City's Department of Transportation ("CDOT") have been "poor," a problem the utility has acknowledged. *Id.* at 20:399-401. Mr. Cheaks testified that the utility's construction management in Chicago's public way has also been "poor." *Id.* at 21:420-425. Examples of Peoples Gas's poor performance cited by Mr. Cheaks include doing work without necessary permits, shutting down a portion of a street without City permission, deviating from designs submitted for CDOT approval, submitting unrealistic construction schedules, applying for permits that were not needed, and applying for permits to do work at locations where the utility had recently finished projects. *Id.* at 23-26:461-510. Due to its apparent inability to comply with City ordinances and regulations, from 2011 through 2014, Peoples Gas has been charged with 67% more violations than the next three highest offenders combined. *Id.* at 30:561-569.

The AG adds that the Liberty Interim Report, as stated by Staff witness Stoller, concluded "there are, in Liberty's opinion, several problems with the way Peoples Gas has conducted AMRP." Staff Ex. 8.0 at 9:171-174. In its briefs, the AG summarized certain of the Liberty auditors' conclusions regarding the current state of the AMRP.[1]

The AG points out that in response to an AG/City Motion to Extend the Schedule in this case to incorporate the results of Liberty's Interim Report and the JA's response to the report, the ALJ issued a ruling requiring the JA (and other parties) to submit supplemental testimony addressing:

[1] The AG's summary of the issues discussed in the Liberty Interim Report are not repeated here because of the Commission's conclusion that the report should remain confidential. The Commission acknowledges that the AG and CUB/City disagree with the Commission's conclusion regarding the confidential treatment of the Interim Report.

> (1) whether the Joint Applicants are aware of the scope and scale of the potential obligations under AMRP; and (2) whether Joint Applicants are ready, willing and able to implement the AMRP consistent with additional remedies as recommended by the Liberty audit.

ALJ Ruling, January 14, 2015.

The AG alleges that the JA's supplemental testimony, as well the other evidence of record, demonstrates that the JA have not shown that they are "ready, willing, and able to implement the AMRP consistent with the additional remedies as recommended by the Liberty audit." In fact, the AG asserts that the JA have shown a startling lack of concern about a multi-billion infrastructure program that has been beset with poor management from its inception and has resulted in substantial cost overruns that threaten to double a typical customer's base rates by 2024. AG Ex. 2.0 at 15:300-306. The AG avers that the JA's apparent indifference to remedying the AMRP's many problems has manifested in many ways.

First, and perhaps most important, the AG explains that the JA have no transition plan for assuming ownership of Peoples Gas and oversight of the very troubled AMRP. This point was made clear in the Joint Applicants' Responses to the March 11, 2015 Commissioner Data Requests ("JA's Responses"), wherein they admitted that no transition plan has been developed. JA's Responses at 2-3. The Commissioners' question on this point sought this information "to ensure a seamless changeover that avoids any diminishment of the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public service both leading up to and after closing the proposed reorganization, if approved." Notice of Commissioners' Data Request at 2. Rather than providing the information requested by the Commission, the Joint Applicants, as City/CUB witness William Cheaks, Jr. aptly put it, "describe[d] aspirational initiatives, not concrete commitments, and their compliance is not readily measurable or enforceable."

City/CUB Ex. 11.0 at 2. Mr. Cheaks added that the Joint Applicants' responses "do not provide any plans or commitments to correct the specific deficiencies in AMRP." *Id.* at 1-2.

The AG states that in an apparent effort to excuse their lack of a transition plan, the JA highlighted a customer outreach program that WEC has initiated in Wisconsin that they say could be made part of the AMRP. JA's Responses at 7. The AG cites AG witness Coppola's comment that while improving customer communication is "admirable," the JA's discussion of customer communication programs is "akin to rearranging the deck chairs on the Titanic while the ship is sinking." *Id.* at 5.

The AG points out that in the last major energy merger case decided by the Commission, the ICC stressed the importance of the transition plans that the Illinois utility and its proposed purchaser had in place so that no "diminishment of the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public utility service" would occur as a result of the acquisition. In that case, Georgia-based AGL Resources Inc. ("AGL") proposed to purchase Nicor Inc., the parent company of Northern Illinois Gas Company ("Nicor"). *AGL Resources Inc., Nicor Inc. and Northern Illinois Gas Company d/b/a Nicor Gas Company, Application for Approval of a Reorganization Pursuant to Section 7-204 of the Illinois Public Utilities Act*, ICC Docket No. 11-0046, Final Order of December 7, 2011 at 4 ("*Nicor Merger Order*").

The AG states that in explaining why the merger in that case would not "diminish the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public utility service," the Commission stressed the significance of the integration planning process the joint applicants in that case conducted:

> That exception concerns the integration planning process the JA have conducted since the Reorganization was announced. Specifically, JA explain, several hundred employees of AGL, NI and NG have worked since January 2011 on understanding and

> meshing the "processes, structures and practices" of the merging entities. JA state that these integration planning endeavors "assess the current state for each and every area of the two companies." The JA further assert that their work on final operating plans will continue "until the Reorganization is closed." … JA underscore that approximately 3500 pages of documentation generated by JA's integration planners were submitted to Staff and presented during the evidentiary hearings in this case.

Id. at 11-12 (citations omitted). The Commission added:

> Beyond their evidence of prior and ongoing operating experience, and of specific pledges in support of future operations, the JA point to the ongoing process of integrating the merging entities, as described above. The fact that the JA are conducting this process with a significant commitment of personnel is itself evidence that service quality will be maintained after reorganization. Indeed, it is, conceptually, exactly what needs to occur to achieve a smooth integration of the merging entities.

Id. at 13.

The AG argues that the Joint Applicants' evidence in this case is the antithesis of AGL/Nicor's presentation. Unlike AGL/Nicor,:

● There is no evidence that the Joint Applicants have conducted "an integration planning process" since the proposed merger was announced.

● There is no evidence that the Joint Applicants have made an effort to mesh the "processes, structures and practices" of the merging entities.

● There is no evidence that the Joint Applicants endeavored to "assess the current state for each and every area of the two companies."

● There is no evidence that the Joint Applicants have committed significant personnel and effort to ensure that "service quality will be maintained" after the reorganization.

Next, the AG states that besides the lack of transition plans, there is another important distinction between the record in this case and the record in the AGL/Nicor merger. In the earlier case, the Commission found that "[a]fter [the] merger, staffing levels will be maintained, generally by the same people in place now." *Id*. at 13-14. In response to the Commissioners'

Data Requests in this case, the JA were unable to identify the person or persons who would be responsible for overseeing the AMRP if the transaction is approved. *See*, *e.g.*, JA's Responses at 3. The Joint Applicants were also unable to describe the process for evaluating whether PGL and Integrys employees currently overseeing the AMRP will be retained or replaced. *Id*. at 2-3; Tr. at 214. Each JA witness – whether a WEC or Integrys employee – who was asked about this important issue - testified that he did not know who would manage the program. *See* Tr. at 84, 256, 314.

Like their question regarding the existence of a transition plan, the Commissioners' Data Requests asked for information on this point "to ensure a seamless changeover that avoids any diminishment of the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public service both leading up to and after closing the proposed reorganization, if approved." The AG notes Mr. Coppola's response to the JA's Responses where he stated that:

> It would have been helpful to hear that a core of current personnel would be retained at least during a multi-month period to help with the transition of responsibilities in order to maintain continuity of work. It also would have been informative if the JA had defined a time frame to evaluate the current staff and management assigned to the AMRP so that the Commissioners and other parties could have garnered some confidence that some real and timely transition plan would emerge soon.

AG Ex. 7.0 at 2. However, the JA provided no such information, and the Commission and the parties are left to wonder when, if ever, the JA will have a transition plan in place to take over the AMRP.

Fourth, in its Interim Report, the AG states that the Liberty auditors found that the proposed merger was having an impact on Peoples Gas's efforts to make changes to the AMRP. The AG explained that WEC apparently was not interested in learning about that remedial activity. Mr. Hesselbach testified that he had not held a single conversation with anyone at

Peoples Gas or Integrys regarding the plans Peoples Gas is developing to modify the pipe replacement program. Tr. at 317. He added that he was not aware of WEC having input into the implementation plans. Tr. at 318. In fact, Mr. Hesselbach stated that WEC could not agree that it would follow the initiatives Peoples Gas has begun to develop, saying doing so would be "imprudent." Tr. at 320-321.

Fifth, the AG arguedsthat the witnesses who testified on behalf of JA in response to the ALJ's Ruling that the JA demonstrate that they are "ready, willing, and able to implement the AMRP consistent with the additional remedies as recommended by the Liberty audit" (ALJ Ruling of January 14, 2015) had minimal familiarity with the AMRP. As to Mr. Leverett, the AG asserted that he admitted that WEC did not request a specific work plan as part of its due diligence review. Tr. at 175-176; AG Cross Ex. 3. He testified that he had not read the entire Liberty Interim Report, choosing to only read the Executive Summary. Tr. at 193-194. In fact, other than reading the Executive Summary, Mr. Leverett's knowledge of the Liberty Interim Report was based on two conversations he had with Mr. Kleczynski, Peoples Gas's President, and Mr. Morrow regarding the utility's plans to respond to the Liberty audit findings. Tr. at 204, 206-208. One of those conversations occurred in February 2015 (Tr. at 204), subsequent to the filing date for the supplemental and supplemental rebuttal testimony that was intended by the ALJ to document that the JA were "ready, willing and able" to assume ownership of the AMRP. Thus, it could not have informed Mr. Leverett's assertion in his supplemental testimony that WEC is "ready, willing, and able" to take on the management of the AMRP. The AG claimes that although Mr. Hesselbach appeared to have greater awareness of the Liberty Interim Report, he has not worked on natural gas projects since the mid-1990s, focusing on electric generation projects since that time. Tr. at 315.

The AG goes on to argue that although Integrys and Peoples Gas are two of the Joint Applicants seeking merger approval, those two entities did not submit supplemental testimony as to whether they are "ready, willing, and able to implement the AMRP consistent with the additional remedies as recommended by the Liberty audit." The lack of any testimony from Peoples Gas is remarkable, particularly because, as AG witness Coppola testified, "Peoples Gas (1) is the company that is implementing the AMRP now, and (2) will continue to be implementing it post-merger, should the proposed acquisition be approved." AG Ex. 6.0 at 5:79-81.

The AG concludes that in response to the ALJ's January 14, 2015 ruling, the JA chose to file the testimony of one witness who had little specific knowledge of the Interim Report and the AMRP and a second witness who has not worked on a gas infrastructure project in 20 years. The Joint Applicants also chose not to file any testimony from a witness or witnesses from the two entities that have knowledge of the AMRP (PGL and Integrys) and the apparently existing PGL plans to implement the changes recommended by the Liberty auditors. Other than the JA's "trust us" approach, there is little in the record to conclude that WEC is "ready, willing, and able to implement the AMRP consistent with the additional remedies as recommended by the Liberty audit."

Finally, the AG argues that the JA's seeming indifference to the AMRP is disconcerting due to the significant impact that the costs of the program have had, and almost certainly will continue to have, on customers' bills. The AG notes that Peoples Gas has stated that the AMRP was the main driver for its need for increased rates in each of its last two rate increase requests. AG Ex. 4.0 at 17:324-326. The AG states that the project's estimated costs have swelled from $2.2 billion in 2009 to $4.6 billion in May, 2013. AG Ex. 2.0 at 6:135-139. And, Peoples Gas's

May, 2013 estimate did not include the cost impact of new City of Chicago regulations scheduled to go effect in January 2014 as well as other factors. *Id*. at 19-20:400-407. Thus, the $4.6 billion price tag is likely to increase. AG witness Coppola projected that the main replacement program will cause the average residential customer's base rates to double from "$555 annually to more than $1,100 per year by 2024." AG Ex. 2.0 at 7:159-161.

2. The Record is Clear that the Joint Applicants Failed to Conduct Due Diligence Regarding the AMRP.

It is undisputed that the Joint Applicants have the burden of satisfying the statutory criteria of Section 7-204 of the Act before the Commission can approve any proposed merger. 220 ILCS 5/7-204. As Staff aptly noted in its Initial Brief, where a statute does not specifically place any burden of proof, courts have uniformly imposed on administrative agencies the common-law rule that the party seeking relief has the burden of proof. Scott v. Dept. of Commerce and Community Affairs, 84 Ill. 2d 42, 53; 416 N.E.2d 1082, 1088; 1981 Ill. Lexis 229 at 14; 48 Ill. Dec. 560 (1981). Staff IB at 3-4.

The AG argues that the record evidence is clear that the Joint Applicants failed in presenting the necessary evidence to satisfy that statutory standard. According to the AG, the Commission's analysis of the evidence must begin with the Joint Applicants' admission that they failed utterly to prove that they are ready and able to step into the shoes of PGL/Integrys to manage the day-to-day operations of Peoples Gas, and in particular to seamlessly oversee the operation and management of the PGL AMRP. The AG argues that from the Commission's perspective in this docket, assessing the quality and depth of the acquiring company's due diligence review is directly relevant to its evaluation of claims by WEC that the reorganization will not adversely affect the utility's ability to perform its duties under the Act. 220 ILCS 5/7-204(b). As Staff witness Lounsberry noted:

> A due diligence audit provides a rare opportunity for the Commission to review an outside party's assessment of a utility's system. The absence of a detailed due diligence report on the Gas Companies infrastructure, especially AMRP, reflects a failure by WE to conduct a complete analysis of Integrys. It also limits Staff's analysis and the information that the Commission has when evaluating the benefits of the merger.

Staff Ex. 2.0 at 22:518-522. According to Mr. Lounsberry, "a thorough due diligence review would look into all aspects of a company, including financial records, personnel, legal and regulatory issues, physical assets, and operational procedures and costs." *Id.* at 18-19:452-454

Whether WEC engaged in an adequate due diligence process has implications for not only shareholders, but utility customers, whose interest the Commission is charged with protecting. 220 ILCS 5/7-204(b)(1)-(7),(f). As Mr. Lounsberry noted, WEC's claims that the resulting combined company "will strengthen the WEC Energy Group's operating companies, including the Gas Companies (PGL and NS), by integrating best practices in distribution operations, larger capital project management, gas supply, system reliability, and customer service" must be scrutinized by the Commission in light of evidence of whether the JA actually understood the capital investment commitments and problems of the companies they seek to acquire. Staff Ex. 2.0 at 19. Most importantly, for purposes of the evaluation required of the Commission under Section 7-204 of the Act, WEC's claim that PGL and NS service will not be negatively impacted by the proposed merger transition from Integrys to WEC ownership must be tested in light of evidence of what WEC understood about the operations of Peoples Gas and North Shore Gas when it made those commitments. Likewise, the JA's claim that "the Reorganization will result in a larger, more diversified, financially strong energy company that, over time, may generate benefits from its increased scale of operations[2]" must be examined

[2] JA Ex. 1.0 at 15:315-317.

through the lens of how well WEC understood the day-to-day operations and infrastructure commitments of Peoples Gas.

The AG notes that it is clear that when WEC began the process of proposing to purchase Integrys and Peoples Gas and North Shore, there was already evidence that the AMRP was a program plagued with problems. The Commission had given its stinging assessment of the program's management in its 2012 Rate Case Order. 2012 Rate Case Order at 61. It was also known that as part of its Order in that case, the Commission had ordered a two-part audit of the AMRP. *Id.* Finally, it was known that Liberty, the Commission's selected auditor, had started the first phase of its assessment of the troubled AMRP. All of these things were known – or should have been known – as WEC began its due diligence examination of Integrys and its subsidiary gas companies.

The record evidence in this case reinforce reveals a troubling lack of due diligence by WEC related to the PGL AMRP, according to the AG, both in terms of a basic understanding of the AMRP as an ongoing infrastructure project within the City of Chicago as well as the past and ongoing problems identified by the Commission and the utility's internal auditors in the operation of the program. At least initially in this case, the Commission Staff identified the lack of due diligence as a troubling deficiency in the JA's evidentiary presentation. Staff Ex. 2.0 at 22-24: 534-582. Mr. Lounsberry concluded, "the Joint Applicants conducted no review to determine the level of effort and expenditure it would take on their part to make any of this happen, assuming they can make any of these changes happen at all." *Id.* Indeed, Mr. Lounsberry characterized the Joint Applicants' due diligence review process as "only …a high level review of Integrys without any detailed review of operating practices of the Gas Companies or of AMRP." *Id.* JA witness Leverett confirmed this conclusion during cross-examination when he stated, "WEC didn't do a specific examination of the AMRP" as part of its due diligence analysis. Tr. at 177.

Importantly, the AG notes that Staff witness Eric Lounsberry's Direct testimony concluded that the Joint Applicants had not met their burden of satisfying Section 7-204(b)(1) of the Act. Staff Ex. 2.0 at 23:561-563. He stated:

> The Joint Applicants claim the proposed reorganization will strengthen the WEC Energy Group's operating companies, including the Gas Companies, by integrating best practices in distribution operations, larger capital project management, gas supply, system reliability, and customer service. However, the Joint Applicants conducted no review to determine the level of effort and expenditure it would take on their part to make any of this happen, assuming they can make any of these changes happen at all. This is especially true of larger capital project management, which is what AMRP clearly requires. Therefore, I conclude that Joint Applicants' claims are broad, unsubstantiated generalizations.
>
> *In my opinion, the AMRP is the most risky capital project undertaken by a utility in Illinois since Commonwealth Edison Company and Illinois Power Company began constructing their nuclear powered generation plants, each of which ultimately cost billions of dollars each to complete. It is very clearly not, as WE has described it above, part of Peoples' Gas "day-to-day" operations.*

Staff Ex. 2.0 at 22:563-576 (emphasis added).

In his criticism of WEC's due diligence process, Mr. Lounsberry further noted that WEC's review of the PGL AMRP consisted of public Integrys investor presentations, the Rider QIP (Qualified Infrastructure Program) filing with the ICC and the Section 9-220.3 statute that authorizes gas utilities to file a QIP rider request. *Id.* at 22. He concluded that none of the JA's responses to data requests indicated that WEC had conducted a thorough due diligence review of the Gas Companies' operating practices or any specific review of PGL's AMRP. *Id.* Importantly, he noted that in his view, "the primary focus of WE's review of AMRP was whether Peoples Gas is allowed to recover AMRP costs through its QIP Rider without the need to file for a rate increase under Section 9-201." *Id.* In addition, the record makes clear that the Joint Applicants at no time requested or reviewed a detailed work plan of the AMRP (to the extent that it existed) as part of their due diligence review. *See* Staff Ex. 2.0 at 23, AG Cross Ex. 3.

The AG notes that AG witness Sebastian Coppola, who performed a detailed assessment of the PGL AMRP and concluded, among other findings, that project costs have doubled since originally approved by the Commission in 2010 due to rampant mismanagement, and that the project lacked an overall plan and any sort of cost controls[3], likewise concluded that WEC failed to conduct due diligence in its bid to acquire Integrys and, in particular, Peoples Gas. He testified, "there is no evidence that the Joint Applicants have performed the due diligence necessary to understand the infrastructure investment rate involved in achieving that deadline, the impact on customer rates, and whether the current AMRP is, in fact, prioritizing the most vulnerable main for replacement." AG Ex. 2.0 at 30-31:604-608.

The Joint Applicants responded by arguing that concern about AMRP and other "on the ground" operations before a reorganization is approved "is not customary." JA Ex. 8.0 (Reed Rebuttal) at 13:260-263. JA witness Reed made clear that in the eyes of WEC, Peoples Gas and its troubled AMRP are but a small cog in the big wheel that is a newly reorganized Wisconsin Energy Corporation:

[3] Mr. Coppola stated that it is likely that over the 20-year life of the program, the total cost of the AMRP will exceed $4.6 billion, as opposed to the $2.2 billion Peoples Gas projected it would cost in 2009. AG Ex. 2.0 at 20. He also concludes that, within the next 10 years, the AMRP will about double the portion of residential customers' gas bills related to base rates if the Joint Applicants are permitted to install infrastructure at the level of costs currently projected under a 2030 timeline. *Id.* at 28. He concluded that PGL practices have contributed to "huge cost overruns, delays in completing projects, and, in my view, a state of mass confusion and uncertainty as to whether or not the critical objectives of increasing safety, system reliability, operating cost reductions, and financial benefits to customers have actually been, or are likely to be accomplished." *Id.* at 20.

> When viewed in the context of the larger transaction, those amounts equal about $300 million per year in capital expenditures on AMRP measured against a total capital program of 1.5 million, so they're about 20 percent of the annual capital budget. And they're also measured for relevance of whether they're material. They're measured against the entire asset base of the company, which is $17 billion. That's about 1.75 percent per year for the capital expenditures on the AMRP as compared to the aggregate enterprise value or asset value of the combined company.

Tr. at 426. JA witness Leverett went so far as to characterize the AG and City/CUB testimony that discussed the AMRP and concerns about future operations under WEC ownership as issues "that are unrelated to the proposed Reorganization." JA Ex. 6.0 at 9:272. The problem with these assumptions, however, is that Peoples Gas ratepayers and, indeed, the Commission, *do* care and *are interested* in the AMRP capital expenditure plans of a WEC-owned Peoples Gas. For example, as noted above, in PGL's 2012 rate case, the Commission ordered that an independent audit of the troubled AMRP be conducted in order to identify and remedy integral operational flaws, including the lack of an overall plan for the project, budget or cost controls.[4] From the ratepayers' perspective, the AMRP has been the primary driver in Peoples Gas's constant rate increase requests. In the four years since PGL initiated the AMRP, Peoples Gas has filed three base rate cases and received approval for increases in rates of $57.8 million, $59.8 million, and $71.1 million.[5] By far, the largest driver of these actual and proposed rate increases has been the actual and forecasted capital investment and expenses tied to the Company's AMRP.[6]

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[4] ICC Docket Nos. 12-0511/0512 (cons.), North Shore Gas Company and Peoples Gas Light & Coke Company– Proposed General Increase in Rates, Order of June 18, 2013 at 61.

[5] ICC Docket No. 11-0280/0281, Order of January 10, 2012 at 237; ICC Docket Nos. 12-0511/12-0512 (cons.), Order on Rehearing of December 18, 2013 at 21; ICC Docket Nos. 14-0224/0225 (cons.), Second Amendatory Order of February 11, 2015 at 4.

[6] ICC Docket No. 11-0281, PGL Ex. 1.0 at 10-11; ICC Docket No. 12-0281, PGL Ex. 1.0 at 3. ("The largest cause of the increase is Peoples Gas' capital investments to improve the reliability of its gas distribution system and the quality of its services. The largest capital investments currently being made by Peoples Gas are for main replacement, in particular the replacement of cast iron and ductile iron gas main in the City of Chicago."); ICC Docket No. 14-0225, PGL Ex. 1.0 at 5. ("The costs that Peoples Gas incurs in order to serve its customers have

When pressed in cross-examination, WEC's justification for its minimalist view of due diligence requirements falls apart, according to the AG. In fact, Mr. Leverett admitted during cross-examination that information regarding capital expenditure budgets for WEC's utility companies are (and should be) a concern for both WEC and its investors. Tr. at 177. He admitted that understanding the projected capital expenditure spending of a utility WEC is acquiring *is,* in fact, important to WEC. Tr. at 178. He further agreed that PGL's AMRP *directly* impacts PGL's level of capital expenditures. *Id.* As for JA witness Reed, he admitted that he did not participate in WEC's due diligence review (Tr. at 372), but conceded that a multiple billion dollar capital expenditure program is significant for PGL and the combined company. Tr. at 429.

The AG states that Mr. Lounsberry, however, inexplicably went on to testify in Rebuttal testimony that he was somehow satisfied that the Joint Applicants now understand the breadth of the infrastructure and operational challenges the AMRP presents to the acquiring company – apparently based on the JA's review of Intervenor and Staff testimony. Staff Ex. 9.0 at 27:653-658. He added that the JA's commitment to "various conditions," including those related to implementation of the Liberty Audit, assuaged him of his early concerns about the quality of the JA's due diligence.

This change in Staff's position is startling, alleges the AG, given the importance of the AMRP to PGL customer service and rate levels, and the Companies' stated view that the AMRP is unrelated to merger approval, the AG states. The AG observes that Staff seems to suggest that it is appropriate for due diligence to be conducted during the middle of a merger proceeding, *after* the decision to acquire a utility has been made. Yet, notes the AG, even JA witness

increased significantly in recent years, due primarily to main replacement and other increased plant investment costs, and increased operating expenses, such as increased costs of pipeline safety and other compliance work.")

Leverett admitted on cross-examination that due diligence typically requires examining an acquired company's infrastructure commitments *before* an acquisition agreement is signed. Tr. at 192-193. That did not take place here.

The AG points out that as Mr. Coppola aptly testified, the AMRP is not a small operational program to be dealt with in post-merger due diligence. Astounded by the JA's response to AMRP concerns and its clear lack of due diligence in reviewing the obligations and problems of the AMRP, Mr. Coppola stated:

> The AMRP is fundamental to the future earning power, reliability and safety of the Peoples Gas delivery system. It is not only material to the entities being acquired, it is essential to the success of the acquisition. The facts (1) that the Commission ordered an audit of the AMRP and (2) that completing the program by 2030 requires investing more than $4 billion in capital expenditures should have triggered a need to perform some significant due diligence. By any reasonable standard, a $4 billion capital program is material in this merger transaction. For the Joint Applicants not to have done a reasonable amount of due diligence of the program in the pre-merger phase raises grave concerns about Wisconsin Energy's understanding of the current state of the AMRP and its priorities and commitments to complete the AMRP in a way that will not harm customers if the merger is approved.

AG Ex. 4.0 at 17-18:333-344. City/CUB witness Cheaks similarly found the JA's level of due diligence lacking, to say the least, noting that it "fails to give the ICC confidence that AMRP will be properly managed and the interests of PGL's ratepayers protected." City/CUB Ex. 3.0 at 46:891-901.

The AG states that Mr. Lounsberry's initial criticism of the JA's due diligence process was the more accurate assessment. This is perhaps best revealed in the Company's own pre-filed testimony and subsequent revelations during cross-examination. For example, despite the evidence presented about the dismal state of the PGL-run AMRP, lead JA witness Leverett proclaimed in Rebuttal testimony that "the proposed Reorganization will leave Peoples Gas (and North Shore) essentially unchanged…." JA Ex. 7.0 at 9:262-264. Moreover, notes the AG, clearly oblivious or indifferent to the endemic problems in Peoples Gas AMRP management and cost control processes, and in no mood to assure the Commission that it intended to ensure any corrective actions relative to the Liberty audit, the JAs intended to convince this Commission to focus instead on its suggested narrow reading of the statute. Leverett testified thus: "While I am not an attorney, it seems that the provisions of Section 7-204 focus on ensuring that a reorganization will not 'diminish' a utility's ability to perform its duties under the Act and provide service to its customers, 'significantly impair' its ability to raise capital and maintain a reasonable capital structure, or cause 'adverse rate impacts.'" *Id.* at 11:316-318.

The AG notes that the JA admit that "Wisconsin Energy's pre-merger due diligence did not include investigation into the specifics of the Gas Companies' 'on-the-ground' operations, such as detailed work plans for the AMRP." JA Brief at 12, citing Leverett Reb., JA Ex. 6.0, 14:385-387; Reed Reb., JA Ex. 8.0, 13:259-268; AG Cross Ex. 3 (JA response to data request AG 4.01). As it turns out, that was an understatement of the JA's level of interest in assessing the day-to-day operations of Peoples Gas, and in particular its immense, $4.6 billion infrastructure project, the AMRP, according to the AG. Section 7-204(b)(1) requires that the Commission examine WEC's ability to ensure that the proposed merger would not diminish PGL's ability to provide adequate, reliable, efficient, safe and least-cost public utility service. The AG suggests that whether WEC is able to immediately step into the role of current PGL/Integrys management – particularly the management team currently overseeing the AMRP – is a critical question for that assessment.

The AG notes that the answer to that query is that WEC is not ready to take the helm of the sinking ship that is the PGL AMRP, the AG states. Even by the end of the case, cross-examination of the JA witnesses revealed a stunning lack of knowledge about the AMRP, according to the AG, again indicative of the lack of adequate due diligence in researching and understanding the operations of Peoples Gas, an inadequate commitment to ensure best practices in the operation of the AMRP, and an inability to ensure a smooth transition that will not negatively impact Peoples Gas's quality of service, reliability, safety and customer rates. Lead JA witness Leverett, who also filed the principal testimony alleging that Joint Applicants were "ready, willing and able" to implement Liberty audit recommendations, and who specifically responded to criticisms of the quality of the due diligence review of PGL by WEC, admitted that WEC:

- Was not aware that PGL lacked any overall plan for the AMRP (Tr. at 187); *see also* ICC Ex. 8.0 Attachment A (Confidential Liberty Interim Report) at 9;
- Performed no analysis of whether PGL had in place formal written guidelines or procedures related to the AMRP (Tr. at 196);
- Could not name who is in charge of the AMRP at Peoples;
- Had no knowledge of the number of miles of main that PGL has replaced to date or has remaining to replace (Tr. at 220);
- Had no understanding of the main ranking index used to prioritize main replacement from a safety and reliability perspective (Tr. at 237);
- Performed no review of PGL's internal PricewaterhouseCoopers audits, which identified operational deficiencies and needed remedial action in the AMRP (Tr. at 182-183);
- Had no communication with Integrys employee and JA witness David Giesler, who is responsible for project planning, execution, control, and close out for the AMRP, and was the JA witness from Peoples Gas responding to Intervenor criticisms of the PGL AMRP (JA Ex. 1.0 at 1:9-10);

- Did not include the JA witness, Andrew Hesselbach in WEC's due diligence review of Integrys/Peoples Gas, even though Mr. Hesselbach sponsored testimony in response to the ALJ's January 14, 2015 directive to file testimony indicating "whether the JA are aware of the scope and scale of the potential obligations under AMRP"; and "whether the JA are ready, willing and able to implement the AMRP consistent with additional remedies as recommended by the Liberty audit") (Tr. at 183);

- Performed no analysis of whether the Staff-requested 2030 AMRP completion date was even feasible (Tr. at 221), despite including it as a Joint Applicant commitment in Rebuttal testimony;

- Had no idea how long an assessment of the feasibility of achieving a 2030 would take (Tr. at 222);

- Had no opinion as to whether the AMRP is currently on track to achieve a 2030 completion date (Tr. at 222).

In fact, the AG points out that the Joint Applicants did not even acknowledge that systemic, critical problems existed in PGL's operation of the AMRP until January 29, 2015, and only following the ALJ's ruling that the Joint Applicants should file supplemental rebuttal and surrebuttal testimony addressing: "(1) whether the Joint Applicants are aware of the scope and scale of the potential obligations under AMRP; and (2) whether Joint Applicants are ready, willing and able to implement the AMRP consistent with additional remedies as recommended by the Liberty audit." *See, gen'ly,* JA Ex. 12.0 (Leverett Supplemental Rebuttal), 13.0 (Hesselbach Supplemental Rebuttal) and 14.0 (Leverett Supplemental Reply). According to the AG, that testimony and the cross-examination of JA witnesses Leverett and Hesselbach regarding that alleged state of readiness to step into the shoes of Peoples Gas and Integrys in overseeing the AMRP and implementation of Liberty audit recommendations revealed a startling lack of readiness to do just that, and clear disinterest in the PGL remedial activity that Mr. Giesler testified is now occurring, according to the AG. Tr. at 263.

The AG argues that this lack of due diligence must inform the Commission's evaluation of the Joint Applicants' commitments, detailed in JA Ex. 15.1 REV, and their claims that they are "ready, willing and able" to implement the final audit recommendations related to PGL's AMRP, due to be released sometime this Spring. More importantly, as discussed further below, it points to an inability to demonstrate that the proposed reorganization will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service, a burden of proof that is required under Section 7-204(b)(1) of the Act.

B. Commission Analysis and Conclusion Regarding Section 7-204(b)(1)

Section 7-204(b) of the Public Utilities Act (the "Act") provides that no reorganization shall take place without prior Commission approval. 220 ILCS 5/7-204(b). Before approving any proposed reorganization, the Commission must find that:

> (1) the proposed reorganization will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service;

The concept of "due diligence" refers to the investigation that is initiated when one company is contemplating acquiring or merging with another company. Staff Ex. 2.0 at 18. According to Staff witness Lounsberry, "a thorough due diligence review would look into all aspects of a company, including financial records, personnel, legal and regulatory issues, physical assets, and operational procedures and costs." *Id.* at 18-19:452-454

Whether WEC engaged in an adequate due diligence process has implications for not only shareholders, but utility customers, whose interest the Commission is charged with protecting. 220 ILCS 5/7-204(b)(1)-(7),(f). As Mr. Lounsberry noted, WEC's claims that the resulting combined company "will strengthen the WEC Energy Group's operating companies, including the Gas Companies (PGL and NS), by integrating best practices in distribution operations, larger capital project management, gas supply, system reliability, and customer service" must be scrutinized by the Commission in light of evidence of whether the JA actually understood the capital investment commitments and problems of the companies they seek to acquire. Staff Ex. 2.0 at 19. Most importantly, for purposes of our evaluation required of the Commission under Section 7-204 of the Act, WEC's claim that PGL and NS service will not be negatively impacted by the proposed merger transition from Integrys to WEC ownership must be tested in light of evidence of what WEC understood about the operations of Peoples Gas and North Shore Gas when it made those commitments.

The Commission is first of all troubled by the clear lack of due diligence on the part of the acquiring company, WEC. As the AG noted in its Reply Brief, it is undisputed fact that PGL has (1) the dubious distinction of having the highest rates in the state, (2) a problem-plagued AMRP, (3) an ongoing independent audit of the AMRP, and (4) a newly opened ICC docket investigating troubling whistle-blower allegations of fraud and mismanagement related to the AMRP (ICC Docket No. 15-0186). Yet, it appears that the Joint Applicants are either stunningly oblivious to these facts or, worse yet, disinterested in improving PGL operations as a condition of merger approval, as perhaps best highlighted in this statement from the JA's Brief, citing testimony from lead JA WEC witness Allen Leverett:

> From the perspective of Peoples Gas' and North Shore's customers, the Reorganization will be seamless, as they will continue to receive high-quality, adequate, safe, and reliable gas service at the same cost as they did before the Reorganization. JA Ex. 1.0 (Leverett Direct) at 16:350-353; Leverett Reb., JA Ex. 6.0, 9:265-268.

JA IB at 4. Cross-examination of the lead WEC witness Leverett revealed a startling lack of knowledge about the basic operations of Peoples Gas. For example, Mr. Leverett knew few, if any details about PGL's AMRP, including information about the Company's Main Ranking

Index ("MRI"), which is used to identify vulnerable mains in the distribution system. Tr. 182-237.

The Commission agrees with the AG that the proposed transaction must be rejected because it does not meet Section 7-204(b)(1)'s requirement that it "will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service." 220 ILCS 7-204(b)(1). The Commission does not reach this decision lightly, but feels compelled to do so because of the remarkable lack of attention the proposed purchasers of the Utilities paid to Peoples Gas's accelerated main replacement program.

As discussed in our review of Section 7-204(b)(7) below, there is ample unrebutted evidence that the AMRP has had, and will continue to have, tremendous impacts on Peoples Gas's customers' bills. Moreover, in the 2012 Rate Case Order, the Commission found that the AMRP had many problems. We stated there that:

> Part of the problem with the AMRP is the lack of detail. Staff examined Peoples' submissions to Staff DR ENG 2.12, which asked for a detailed explanation of its five-year plan for the AMRP, including all costs. They found: "There is no discussion of costs in the White Paper. There is no discussion of resource requirements or project management. The response to Staff DR ENG 2.12 states that the AMRP budget for 2013 is $220.75 million, but does not explain how Peoples arrived at that number and Attachment 01, the White Paper, does not address the issue either." *Id.* at 19. Additionally, Peoples also stated that they "have not determined the funding level past the year 2013". *Id.* Attachment 20.02.

2012 Rate Case Order at 61. Because of the problems identified in our Order, ordered "a two-phase investigation of the AMRP [be conducted] under Section 8-102 of the Act (220 ILCS 5/8-102) ending in a public document report." *Id.*

The record shows that the problems with the AMRP continue. Among other problems, Mr. Coppola testified that a 2012 internal review of Peoples Gas's AMRP project management conducted by PWC "identified several deficiencies and 23 areas where improvements needed to be made." AG Ex. 2.0 at 16-17:341-342. Mr. Coppola pointed out that "as of October 2014, two years later, none of these improvements have been completed." *Id.* at 17:342-343. Mr. Coppola added that Peoples Gas and Integrys admit that they "have not formally defined a future state operating model or project delivery strategy in conjunction with the Rider QIP, or developed associated processes and controls." *Id.* at 17:350-353; AG Ex. 2.2. Mr. Coppola concluded that

> The scale of the AMRP seems to have overwhelmed the utility's resources. It has not proved itself capable of managing an accelerated main replacement program that is more than double in scope from what PGL was managing historically. The demands on the City of Chicago to respond to the increased activity of the AMRP also have taxed the resources of the City. The result has been huge cost overruns, delays in completing projects, and, in my view, a state of mass confusion and uncertainty as to whether or not the critical objectives of increasing safety, system reliability, operating cost reductions, and financial benefits to customers have actually been, or are likely to be accomplished.

AG Ex. 2.0 at 20:410-418.[7]

Despite the significant cost impacts and the problem-plagued history of the AMRP, the JA stated in response to the Commissioners' March 11, 2015 Data Requests that they the JA have no transition plan for assuming ownership of Peoples Gas and oversight of the AMRP. JA's Responses at 2-3. The Commissioners' question on this point sought this information "to ensure a seamless changeover that avoids any diminishment of the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public service both leading up to and after closing the proposed reorganization, if approved." Notice of Commissioners' Data Request at 2. Rather than providing the information requested by the Commission, the Joint Applicants, as City/CUB witness William Cheaks, Jr. aptly put it, "describe[d] aspirational initiatives, not

[7] City/CUB witness William Cheaks, Jr. and the Liberty auditors also identified numerous problems with the way Peoples Gas has conducted AMRP.

concrete commitments, and their compliance is not readily measurable or enforceable." City/CUB Ex. 11.0 at 2. Mr. Cheaks added that the Joint Applicants' responses "do not provide any plans or commitments to correct the specific deficiencies in AMRP." *Id*. at 1-2.

The JA's lack of a transition plan is particularly concerning because in our Order in the last major energy merger case, we stressed the importance of the transition plans that the Illinois utility and its proposed purchaser had in place so that no "diminishment of the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public utility service" would occur as a result of the acquisition. In that case, AGL proposed to purchase Nicor Inc., the parent company Nicor. Certain parties argued that AGL/Nicor failed to meet the requirements of Section 7-204(b)(1) because their case "principally consists of recitations about NG's pre-merger service quality, AGL's track record with previous mergers, declarations of good intentions and a pledge not to reduce NG's aggregate staffing for three years." Nicor Merger Order at 11.

In our Order in that case, we concluded that the extensive integration planning process AGL/Nicor conducted addressed the legitimate concerns raised regarding the sufficiency of AGL/Nicor's evidentiary presentation. In particular, we stated:

> That exception concerns the integration planning process the JA have conducted since the Reorganization was announced. Specifically, JA explain, several hundred employees of AGL, NI and NG have worked since January 2011 on understanding and meshing the "processes, structures and practices" of the merging entities. JA state that these integration planning endeavors "assess the current state for each and every area of the two companies." The JA further assert that their work on final operating plans will continue "until the Reorganization is closed." … JA underscore that approximately 3500 pages of documentation generated by JA's integration planners were submitted to Staff and presented during the evidentiary hearings in this case.

Id. at 11-12 (citations omitted). We added:

> Beyond their evidence of prior and ongoing operating experience, and of specific pledges in support of future operations, the JA point to the ongoing process of integrating the merging entities, as described above. The fact that the JA are conducting this process with a significant commitment of personnel is itself evidence that service quality will be maintained after reorganization. Indeed, it is, conceptually, exactly what needs to occur to achieve a smooth integration of the merging entities.

Id. at 13.

Similar to the concerns raised in the AGL/Nicor case, the AG and City/CUB argued that the Joint Applicants failed to show that their plans regarding the AMRP satisfy the requirements of Section 7-204(b)(1). However, unlike the prior case, the Joint Applicants' evidence in this case is the antithesis of AGL/Nicor's presentation. Unlike AGL/Nicor,:

● There is no evidence that the Joint Applicants have conducted "an integration planning process" since the proposed merger was announced.

● There is no evidence that the Joint Applicants have made an effort to mesh the "processes, structures and practices" of the merging entities.

● There is no evidence that the Joint Applicants endeavored to "assess the current state for each and every area of the two companies."

● There is no evidence that the Joint Applicants have committed significant personnel and effort to ensure that "service quality will be maintained" after the reorganization.

In addition, to not having a transition plan, the Joint Applicants were unable to identify the person or persons who would be responsible for overseeing the AMRP if the transaction is approved. *See*, *e.g.*, JA's Responses at 3. The Joint Applicants were also unable to describe the process for evaluating whether PGL and Integrys employees currently overseeing the AMRP will be retained or replaced. *Id.* at 2-3; Tr. at 214. Each JA witness – whether a WEC or Integrys employee – who was asked about this important issue - testified that he did not know who would manage the program. *See* Tr. at 84, 256, 314.

In sum, the JA have shown a startling lack of concern about a multi-billion infrastructure program that has been beset with poor management from its inception and has resulted in substantial cost overruns that threaten to double a typical customer's base rates by 2024. AG Ex. 2.0 at 15:300-306. The Commission concludes that the Joint Applicants' seeming indifference regarding the current and future state of the AMRP requires that the Commission reject the proposed transaction because we find that the Joint Applicants did not prove that it "will not diminish the utility's ability to provide adequate, reliable, efficient, safe and least-cost public utility service." 220 ILCS 7-204(b)(1).

Finally, we are mindful of the AG's statement in their Initial Brief that the Commission cannot protect the interests of the utilities and their customers, as it is required to do under Sections 7-204, if it is investigating allegations of wrongdoing involving WEC and other members of the Joint Applicants in Docket No. 15-0186 while simultaneously moving ahead with a decision as to whether WEC should be permitted to acquire the Gas Companies in this docket. Moving forward to approve a merger under these circumstances is contrary to the ICC's obligation to protect the interests of utility customers. 220 ILCS 5/ 7-204(b),(f). Without having completed its investigation into the alleged wrongdoing, the Commission simply cannot be assured that the transition will not prolong or exacerbate dysfunction in PGL's AMRP. Indeed, the Commission has already asserted a connection between the merger and the investigation. Docket No. 15-0186, Corrected Initiating Order at 1.

[IF THE COMMISSION REJECTS THE AG'S POSITION THAT THE PROPOSED TRANSACTION SHOULD BE REJECTED BECAUSE IT FAILS TO MEET SECTION 7-204(b)(1), THEN, AT A MINIMUM, THE COMMISSION SHOULD ADOPT THE

CONDITIONS THAT WERE INCLUDED AS APPENDIX C TO THE AG'S INITIAL BRIEF.]

III. The Proposed Reorganization Violates The Requirement of Section 7-204(b)(7) to Not Adversely Impact Retail Customer Rates.

A. AG's Position

1. The JA Propose to Increase the Pace of AMRP Construction Activity Far Above Trend In A Way That Will Increase Customer Rates.

Both the ICC Staff and the Joint Applicants propose that the Joint Applicants commit as part of the proposed reorganization to complete the AMRP by 2030; the Joint Applicants add the caveat that the commitment would be conditioned on "appropriate cost recovery." The AG alleges that this commitment would virtually ensure that PGL's rates will continue to increase at the alarming rate that persists currently – and will continue to do so without any guarantee that the 2030 date will ensure the safety and integrity of the PGL distribution system.

The AG states that when the Commission originally ordered the AMRP in PGL's 2009 rate case, Docket Nos. 09-0166/0167 (cons.) (the "2009 Rate Case"), the Commission first approved the institution of an infrastructure cost recovery rider known as Rider ICR for purposes of supporting an accelerated main replacement program for PGL's pipelines.[8] The Commission then approved PGL's proposed AMRP and required completion of the program by 2030 – an end date that PGL had proposed in an effort to secure approval of the rider.[9]

The AG states that since the Commission first issued that order more than five years ago, Peoples Gas has fallen badly behind schedule in its AMRP; PGL's current pace of main

[8] Order, Docket Nos. 09-0166/0167 (cons.) at 194.

[9] *Id.* at 196.

replacement puts it far off any putative 2030 completion date. The AG states that its witness, Mr. Coppola, found in his Direct testimony that, while the accelerated program approved in the 2009 Rate Case entailed[10] the installation of 164 miles of new coated steel and plastic pipe annually, it had installed only 103 miles in 2011, 136 miles in 2012, and 98 miles in 2013. AG Ex. 2.0 at 13-14:282-287. Mr. Coppola found that PGL's "inability to achieve the target installation of 164 miles of new main per year called for in the current program means that it will need to install even more in coming years in order to complete the program by 2030. This is not likely to occur. The result would certainly be further cost overruns that will drive the final cost of AMRP even higher." AG Ex. 2.0 at 30:600-604. The "further cost overruns" that Mr. Coppola alludes to are beyond the existing cost overruns that have inflated the estimated total construction cost of the AMRP from around \$2.2 billion, as projected in the 2009 Rate Case, to around \$4.6 billion in May, 2013. AG Ex. 2.0 at 19:394-399.

The AG argues that the Commission's directive to have Peoples Gas complete the AMRP by 2030 was made only in the context of approving Rider ICR, as discussed above. Rider ICR was overturned by the Appellate Court in 2011. *People ex rel. Madigan v. Illinois Commerce Comm'n,* 2011 IL App (1st) 100654 (Sep. 30, 2011), at ¶ 42. The AG then argues that the Commission recognized that the 2030 completion date was no longer operative in its next rate order for Peoples Gas, Docket Nos. 12-0511/0512 (cons.), in which it noted (relying on Staff witness Buxton's testimony) PGL's lack of progress on the AMRP[11], and it ordered an investigation to determine the "shortest reasonable time" in which the AMRP could be

[10] *See* AG Ex. 2.0 at 12:249 (citing Docket No. 09-0167, PGL Ex. SDM-1.15).

[11] The Commission's Order in that proceeding expressly relied on the testimony of Staff witness Buxton, who found that "[t]here is no reason for the Commission to believe that Peoples can complete its AMRP in 20 years as it convinced the Commission it should back in 2009." Staff Ex. 2.0 at 16:375-377; Order, Docket Nos. 12-0511/0512 (cons.), June 18, 2013, at 61 ("[f]or reasons detailed in Staff witness Buxton's rebuttal testimony . . . this Commission adopts Staff's proposed two-phase investigation of the AMRP").

completed.[12] AG witness Coppola found in this proceeding that he has "seen no evidence in this case that leads me to believe that Mr. Buxton's conclusions are no longer true. The level of construction activity that Peoples Gas has undertaken to implement the AMRP is taxing its resources and capabilities." AG Ex. 4.0 at 31:591-593.

The AG asserts that the record is clear that if Peoples Gas were to now follow through on a goal of completing the AMRP by 2030, the effect on residential customer rates would be large and financially burdensome for Chicago residents. Calculations by AG witness Coppola in this case show that, if a 2030 completion date for the AMRP is assumed, the incremental contribution of AMRP costs – including rate base effects and Rider QIP recovery – to the typical residential customer bill will reach $529 by 2023 (up from $10 in 2011 and $180 today). AG Ex. 2.0 at 28-29. The AG notes that for context, a typical residential customer's annual PGL bill as of 2013 includes around $555 related to base rates. *Id.* at 28:567-568. The AG states that no JA witness refuted Mr. Coppola's findings.

The AG notes that in the four years since the Commission approved the AMRP in 2010, Peoples Gas has filed three base rate cases and received approval for increases in rates of $57.8 million[13], $59.8 million[14], and $71.1 million.[15] As the AG alleges, by far the largest driver of these actual and proposed rate increases has been the actual and forecasted capital investment and expenses tied to the Company's AMRP[16], due largely to the gross mismanagement of the

[12] Order, Docket Nos. 12-0511/0512 (cons.), June 18, 2013, at 61.

[13] ICC Docket No. 11-0280/0281, Order of January 10, 2012 at 237.

[14] ICC Docket No. 12-0511/12-0512, Order on Rehearing of December 18, 2013 at 21.

[15] ICC Docket No. 14-0224/0225, Order of January 28, 2015.

[16] ICC Docket No. 11-0281, PGL Ex. 1.0 at 10-11; ICC Docket No. 12-0281, PGL Ex. 1.0 at 3. ("The largest cause of the increase is Peoples Gas' capital investments to improve the reliability of its gas distribution system and the quality of its services. The largest capital investments currently being made by Peoples Gas are for main replacement, in particular the replacement of cast iron and ductile iron gas main in the City of Chicago."); ICC Docket No. 14-0225, PGL Ex. 1.0 at 5. ("The costs that Peoples Gas incurs in order to serve its customers have

project that has been meticulously documented by AG and City/CUB witnesses in this case and the Liberty Interim Audit Report. The AG states that those facts are only made worse by the JA's admission that no transition plan exists for WEC to assume management of the AMRP operation.

The AG observes that the Joint Applicants now propose to resurrect a completion date that they have proven to be unachievable: as commitment no. 5 of their list of conditions and commitments, they propose that after a hypothetical merger, PGL will commit to continue the AMRP, assuming it "receives and continues to receive appropriate cost recovery," with a planned 2030 completion date. PGL Ex. 15.1 REV at 1. Similarly, Staff witness Lounsberry recommends that the Commission require the JA to "reaffirm Peoples Gas' commitment from the 2009 Rate Cases to complete the AMRP by 2030" (Staff Ex. 9.0 at 15:393-395), and Staff witness Stoller argues that the AMRP completion date of 2030 originally ordered in the 2009 Rate Case Order should be ordered anew as part of the proposed merger. Staff Ex. 8.0 at 8:159.

The AG argues that both Section 7-204(b)(1) and Section 7-204(b)(7) of the Act are salient in evaluating whether the Commission should order such a commitment to a 2030 completion date. Subsection (b)(1) requires that a reorganization not diminish a utility's ability to provide (*inter alia*) least-cost service; subsection (b)(7) requires that a reorganization be not likely to result in any adverse rate impacts for retail customers. The AG notes that as Mr. Coppola's findings discussed above show, a re-commitment to the 2030 completion date would scale the AMRP far beyond PGL's capabilities, requiring it to expand its construction activities at a runaway pace that, if history is any guide, will lead to large cost overruns. The AG argues that PGL is not currently conducting the AMRP on a pace anywhere close to completing the

increased significantly in recent years, due primarily to main replacement and other increased plant investment costs, and increased operating expenses, such as increased costs of pipeline safety and other compliance work.")

work by 2030 and has shown no plans in this proceeding for how it might cost-effectively accelerate its pace of activity commensurate with such an ambitious goal. The AG further suggests that it was, in part, PGL's poor track record over its first two years of AMRP activity in 2011 and 2012 that led the Commission to order the Liberty audit in its 2012 Rate Case order.[17] Thus, the AG argues that if this reorganization is approved and if it entails a re-commitment to the 2030 completion timeline, accelerating the pace of the project over that of the *status quo* would lead to severe rate impacts for retail customers, violating the reorganization approval standard of Section 7-204(b)(7).

Thus, suggests the AG, a merger without a reassessment of what AMRP pace is achievable would diminish the provision of least-cost service and would have adverse retail rate impacts; the Commission should not approve such a merger. The AG avers that the 2030 date was originally selected somewhat arbitrarily in the 2009 Rate Case without any consideration of optimizing safety or minimizing the effect on customer rates. Staff witness Lounsberry admitted during cross-examination that neither he nor anyone at Staff had conducted an analysis of how the 2030 would impact customer rates. Tr. at 566:1-567:2. The AG argues that the Joint Applicants' promise to resurrect the 2030 AMRP completion date without a realistic assessment of whether that date is achievable would have clear, adverse rate impacts on PGL retail customers – a phenomenon Section 7-204(b)(7) prohibits for any merger applicant.

2. The Joint Applicants' Poorly-Defined Request for "Appropriate Cost Recovery" Is a Harbinger of the Rate Shock To Come Should the Commission Approve Their Proposed AMRP Completion Date.

[17] The Commission's 2012 Rate Case Order based its decision to order the AMRP audit on the "reasons detailed in Staff witness Buxton's rebuttal testimony . . . immediately above"; the summary of Mr. Buxton's testimony immediately above in the order's Analysis and Conclusion section included his point that, as of the time of that 2012 Rate Case, the AMRP was behind schedule. Order, Docket Nos. 12-0511/0512 (cons.), June 18, 2013, at 61.

The AG notes that JA witness Schott stated in his Surrebuttal testimony that "appropriate cost recovery" is "linked" to PGL's intention to complete the AMRP by 2030 (AG Ex. 18.0 at 3:47-49) and that JA witness Mr. Leverett added the identical caveat of "appropriate cost recovery" in his Surrebuttal testimony. JA Ex. 15.0 at 9:182-184. The People sought to clarify the meaning of "appropriate cost recovery" through discovery and cross-examination to identify exactly what circumstances would cause the JA's proposed commitment to be effective. The AG notes that in discovery, Mr. Schott stated that, after Rider QIP[18] expires after 2023 pursuant to Section 9-220.3 of the Act, appropriate cost recovery could come through rate case filings, but that "[w]hat the appropriate cost recovery is in future years remains to be seen." AG Cross Ex. 1 at 1. As the AG observes, invited to clarify the precise type of rate case treatment he was referring to, Mr. Schott stated in cross-examination only that he did not feel comfortable answering a question about events nine years hence. Tr. at 98:18-99:3. The AG notes that Mr. Schott mentioned several factors such as "the amount of dollars to be spent, the current regulatory environment, the current financial environment, [and] the current cost projections at the time" (Tr. at 100:2-5) that would inform the definition of "appropriate" cost recovery, but declined to "speculate" as to what "appropriate" cost recovery through a Commission rate order might look like. Tr. at 100:5-8.

The AG alleges that putting aside the inappropriateness of saddling both Peoples Gas and its ratepayers with constant rate increases in order to achieve the unsupported 2030 deadline, as discussed further below, the Commission should not approve a merger with an ambiguous condition whose predicate has not been clearly defined. As the AG puts it, the Joint Applicants

[18] PGL's Rider QIP, approved by the Commission in 2014 pursuant to Section 9-220.3 of the Act, permits Peoples Gas to recover a return of and on qualifying infrastructure investment, including its AMRP investments, through a monthly surcharge on customer bills. 220 ILCS 5/9-220.3.

appear to be deliberately leaving the meaning of "appropriate cost recovery" unclear so that they may escape the obligation of the now-discredited 2030 completion date at a future time of their choosing if a Commission rate order is not to their liking. The AG argues that the JA's unwavering emphasis on gaining "appropriate" cost recovery for AMRP activity suggests that they value the 2030 date not because it is important to optimize public safety, but only to the extent that adding this condition to the merger can improve their profitability. Meanwhile, according to the AG, the extreme acceleration of construction activity within the next 5-8 years that would be required to catch up with a 2030 completion date would cause large adverse retail rate impacts, as noted above – all with an uncertain public benefit. According to the AG, the JA's poorly clarified qualifications for meeting the targeted date would make a 2030 timetable highly unpredictable. The AG argues that the Commission must not impose such a one-sided condition that puts great burden upon ratepayers and relieves PGL of any risk associated with the acceleration – particularly in light of the lack of any tangible, safety-related justification for that particular date and the resulting rate shock that promises to accompany efforts to meet that target.

3. Evidence Shows PGL Has Not and Cannot Keep Pace With the Proposed Completion Date, and the Commission Should Order PGL to Run the AMRP Consistent With Its Capabilities.

The AG alleges that the evidence shows that Peoples Gas simply has been unable to manage an AMRP with a 2030 completion date, and a condition in this proceeding that requires a resumption of that goal would violate the statutory requirements of maintaining least-cost service and causing no adverse retail rate impacts. 220 ILCS 5/7-204(b)(1), (b)(7). AG witness Coppola concluded in his Direct testimony that "[t]he scale of the AMRP seems to have overwhelmed the utility's resources." AG Ex. 2.0 at 20:410. The AG further notes that after reviewing the Liberty Interim Report, Mr. Coppola concluded that the "lack of proper on-site management of the program, the hesitancy on the part of senior level management to make decisions about the organization and structural changes to the program, compounded by cost overruns and delays in completing scheduled projects, all point to an inability to complete the AMRP by 2030." AG Ex. 5.0 (Coppola Supplemental Direct) at 15:317-321.

The AG next observes that Mr. Coppola testified that "[t]he Joint Applicants, particularly Wisconsin Energy, if the merger is approved, face a monumental task to get the program on the right footing, and make up for the lost ground identified in the Interim Audit Report. Continuing to believe that 2030 is an achievable completion date is neither realistic nor advisable in achieving a cost-effective implementation, regardless of any claims the Joint Applicants might make that they will endeavor to do so." *Id.* at 15:322-329.

The AG notes that Mr. Coppola also observed that holding the Joint Applicants to a 2030 completion date for the AMRP will not "achieve completing the program 'at the lowest reasonable cost' – one of the listed goals of the Liberty audit examination." *Id.* The AG also notes that as Mr. Coppola noted in testimony, the Liberty Interim Report does not mention anywhere in its pages a goal of completing the AMRP by 2030. AG Ex. 5.0 at 15:333-16:334. According to the AG, the Commission-hired auditors have not thus far recommended any acceleration of the AMRP to a 2030 completion timeline, and the Commission should not second-guess the auditors by imposing such a condition.

The AG observes that Staff witness Stoller filed Supplemental Reply testimony solely to claim that "[i]t is irrelevant that Liberty did not mention the end date of AMRP in its Interim Report." Staff Ex. 15.0 at 2:18-19. Mr. Stoller claimed that Liberty's task in its ongoing audit is, *inter alia*, "to make recommendations regarding how [PGL] can get back on schedule to complete AMRP by 2030." However, the AG avers that the evidence simply does not support Mr. Stoller's claim that Liberty was hired by the Commission with a goal of moving the AMRP toward completion on that particular date. The AG notes that as Mr. Stoller admitted in a discovery response, the Request for Proposals ("RFP") that initiated the audit now being conducted by Liberty provided that the audit should "help ensure that Peoples completes its AMRP in the shortest reasonable time and at the lowest reasonable cost," but did not ask the prospective auditor to consider the constraint that the "shortest reasonable time" cannot end after 2030. AG Cross Ex. 12 at 1. The AG states that Mr. Stoller also admitted in discovery (AG Cross Ex. 12 at 2) that the "shortest reasonable time" and "reasonable cost" language from the RFP echoes recommendations made in the 2012 Rate Case by Staff witness Buxton, on which the Commission based its final directive to initiate the AMRP audit. (Order, Docket Nos. 12-0511/0512 (cons.), June 18, 2013, at 61.) Moreover, as the AG notes, Mr. Stoller admitted that he does not deem it impossible that Liberty might conclude that the "shortest reasonable time" for completion of the AMRP is a time frame ending after 2030, and he also admitted that Liberty's task of determining the AMRP's likely completion date was not constrained by any condition that the likely completion date could not be after 2030 (AG Cross Ex. 12 at 1, 4); he also admitted that nowhere in the RFP that initiated the audit, other than one reference to a calculation of a pipe replacement pace for a 2030 completion, is there any reference to a 2030 completion date or a 20-year timeline, or to the aforementioned pipe replacement pace calculation. AG Cross Ex. 12 at 3.

4. Neither Staff Nor the JA Conducted Any Rate Impact Analysis Related to the AMRP Completion Date.

The AG alleges that while the Joint Applicants have stated repeatedly that they will commit to complete the AMRP by 2030 (with "appropriate cost recovery"), they have not explained how they matched that goal with the Section 7-204 statutory standards discussed above. The AG notes that as JA witness Mr. Schott agreed in cross-examination, an effectively managed AMRP should minimize the impact on customer rates. Tr. at 95:5-11. The AG states that Mr. Schott, Chief Financial Officer of Integrys Energy Group, stated during cross-examination that (using his example) near-term customer rates would be lower when $100 million is prudently spent in a given year on capital expenditure, compared to capital expenditure of $200 million (Tr. at 104:19-105:10), and he agreed generally that the annual rate of AMRP investment increases customer rates in the near term. Tr. at 105:16-106:1.

The AG notes that despite this correlation, JA witness Mr. Lauber, who is Vice President and Treasurer of WEC, stated during cross-examination that WEC did not ask PGL or Integrys to calculate a rate impact associated with different AMRP completion timelines. Tr. at 462:9-14. Similarly, as the AG notes, Mr. Leverett, President of WEC, stated that neither he nor any other JA witness has performed any recent analysis or assessment to conclude that the 2030 completion date is still feasible and achievable in a cost-effective manner for ratepayers. Tr. at 221:2-7. Additionally, as Mr. Coppola found, "there is no evidence that the Joint Applicants have performed the due diligence necessary to understand the infrastructure investment rate involved in achieving that [2030] deadline [and] the impact on customer rate." *Id.* at 30:604-606.

The AG states that Staff witness Mr. Lounsberry similarly agreed during cross-examination that his recommendation on page 15 of his Rebuttal testimony, Staff Ex. 9.0, that the Joint Applicants should be required as a merger condition to complete the AMRP by 2030 was based solely on his reading of the 2009 Rate Case order and not on any analysis of customer rate impacts.[19] Tr. at 566:1-567:2. As the AG notes, Mr. Stoller also admitted in a discovery response that he did not consider rate impacts to PGL ratepayers associated with his recommendation to re-commit to the 2030 completion date ordered by the Commission in Docket Nos. 09-0166/0167 (cons.). AG Cross Ex. 13. Furthermore, as the AG observes, Mr. Lounsberry similarly admitted in cross-examination that neither he nor any Staff witness has conducted any analysis as to whether the proposed merger could impact AMRP management in a way that could affect customer rates, and he also conceded that neither he nor anyone in the ICC Staff has conducted any independent analysis of the appropriate completion date for the AMRP. Tr. at 516:17-20. Indeed, as the AG states, no witness in this case has attempted to show that, even under the limited criteria offered by PGL witness Marano in the 2009 Rate Case (discussed below), 2030 is still a manageable or appropriate completion date.

According to the AG, in light of the General Assembly's statutory mandate in Section 7-204(b)(7) of the Act to consider retail rate impacts, it is difficult to see how the Commission could approve this proposed reorganization with a 2030 AMRP completion condition when the *only* rate impact study related to the proposed condition, presented by AG witness Coppola, suggests that customer rates would roughly double, before considering any non-AMRP factors that inform the setting of rates, within the next decade if the 2030 completion date is required.

5. The Commission Did Not Choose A 2030 Completion Date In The 2009 Rate Case As A Pipeline Safety Optimization Strategy.

According to the AG, the evidence is clear that neither safety nor reliability are linked to the proposed 2030 completion timeline. The AG notes that as JA witness Schott observed in his

[19] A failure to investigate rate impacts is not the only infirmity with Mr. Lounsberry's recommendation. Mr. Lounsberry admitted in cross-examination that the ICC Staff did not perform any safety or engineering studies to arrive at its recommendation in the 2009 Rate Case or in *this* case that a 2030 completion date was appropriate. Tr. at 569:8-18. He also admitted that Staff has not conducted any analysis or investigation to determine that 2030 is an optimal completion date in terms of management issues. Tr. at 569:19:570:2.

Surrebuttal testimony, the Commission's decision authorizing the AMRP with a 2030 targeted completion date in its 2009 Rate Case was based on the testimony of PGL witness Mr. Salvatore Marano, who provided *cost-benefit* analyses for a possible accelerated main replacement program using three possible completion dates: 2025, 2030, and 2035 – and then from those alternatives concluded that a 2030 completion date was most feasible. JA Ex. 18.0 at 3:52-57. The AG notes that a careful look at the direct testimony filed by Mr. Marano in the 2009 Rate Case regarding a proposed 2030 completion date shows that he focused *only* on cost-benefit analyses and did not consider customer rate impacts, pipeline safety issues, or the Company's ability to manage an accelerated program. AG Ex. 4.0 at 30:577-579; AG Cross Exhibit 2 at 51-59.[20,21] The AG states that in light of the Commission's decision calculus from the 2009 Rate Case, AG witness Coppola correctly noted in his Rebuttal testimony that there is nothing "magical or critical" about a 2030 completion date. AG Ex. 4.0 at 30:577.

While Mr. Stoller alleged in his Rebuttal testimony that "AMRP was not ordered by the Commission for reasons other than pipeline safety" (Staff Ex. 8.0 at 8:153), the AG notes that he later admitted in cross-examination that he was not a Commissioner at the time of the 2009 Rate Case order and agreed that he is not suggesting that he is a legal expert in the interpretation of prior ICC orders. Tr. at 500:8-501:3. In fact, as Mr. Stoller agreed during cross-examination, the Commission approved Rider ICR, which enabled PGL to collect a return of and on AMRP investment over a designated dollar amount each year between rate cases, at the same time as it ordered a 2030 completion date in the Company's 2009 Rate Case order. Tr. at 504:12-20. The AG notes that Mr. Stoller also agreed (Tr. at 506:21) that the Commission's 2009 Rate Case

[20] The cited pages represent pages 49-57 of PGL Ex. SDM-1.0 Rev. from Docket No. 09-0167.

[21] Page 51 of the cross exhibit (page 49 of the Marano testimony) at line 948 poses the question: "How was the basis for the proposed accelerated replacement period determined?" The discussion and analyses on the following eight pages focus only on purported cost savings.

order expressly rejected "Staff's persistent claim that Rider ICR is not needed."[22] According to the AG, the Commission's 2009 Rate Case order speaks for itself and clearly demonstrates that it approved the 2030 AMRP completion date in the context of also approving Rider ICR. The AG observes that as Mr. Stoller agreed, after the Illinois Appellate Court reversed the Commission's approval of Rider ICR in September, 2011, Peoples Gas was unable to collect a return of and on AMRP investment between rate cases until the time in 2014 when Rider QIP was initiated pursuant to the new Section 9-220.3 of the Act. Tr. at 507-508.

The AG advances the proposition that Mr. Stoller's Direct testimony from the 2009 Rate Case shows that the genesis of his support for a 2030 completion date was nuanced and based on the expectation of further Commission review. There, Mr. Stoller recommended that (1) Peoples Gas should be ordered to conduct an in-depth study of the (then-proposed) AMRP since the program appears to be necessary for the long-term safety of PGL's system; (2) PGL should present the Commission with an AMRP implementation plan in a separate docket, with the plan to be analyzed by an independent consultant, and obtain Commission approval before commencing the AMRP; and (3) following Commission approval, PGL should be ordered to return to the Commission with updated analysis of the AMRP every three years. Tr. at 511-512. The AG suggests that the Commission looked to Mr. Stoller's recommendations in the 2009 Rate Case in formulating its conclusion in that case that the AMRP should be concluded by 2030.[23] The AG notes, however, that as Mr. Stoller admitted under cross-examination in this case, the Commission never adopted his second or third recommendation from his 2009 Rate Case testimony. Tr. at 513. The AG argues that it is not clear how Mr. Stoller's 2030 completion

[22] Order, Docket Nos. 09-0166/0167 (cons.), Jan. 21, 2010, at 194.

[23] "The testimony of Mr. Stoller confirms for the Commission what it should do in terms of Rider ICR." Order, Docket Nos. 09-0166/0167, Jan. 21, 2010, at 194.

date recommendation is still tenable when the Commission never executed the second and third steps that Mr. Stoller recommended in his 2009 Rate Case testimony. The AG deems it also noteworthy that Mr. Stoller admitted in this case that he performed no analysis of the impact on customer rates at the time of the 2009 Rate Case, and he did not know if any other Staff member did. Tr. at 517:17-21.

The AG asserts that Mr. Stoller's support for the 2030 completion date is complicated by looking to his statements in the evidentiary hearing of Docket Nos. 09-0166/0167 (cons.), where he admitted that 2030 is not a "magic bullet" and is not necessarily the year that the AMRP must be completed. AG Cross Exhibit 15 at 15; Tr. at 514:10-20. The AG notes that Mr. Stoller admitted in that 2009 hearing that no evidence in that 2009 Rate Case supported the notion that the AMRP must be completed by 2030 (AG Cross Exhibit 15 at 15; Tr. at 515:1-4) and that he also admitted that he did not "know if it's 2029 or 2030 or 2031." AG Cross Exhibit 15 at 15; Tr. at 515:17-22. Finally, Mr. Stoller also admitted in that 2009 hearing that the issue of a particular completion date would be something that should be addressed in the future ICC proceeding that he had recommended in his Direct testimony in that case. AG Cross Exhibit 15 at 15; Tr. at 516: 3-10. The AG avers that if the Commission wished to rely in *this* proceeding on Mr. Stoller's position as it determines an appropriate AMRP completion date, Mr. Stoller's statements under cross-examination and re-direct examination in the 2009 Rate Case do not provide sturdy ground for a finding that a 2030 completion date is imperative. In short, according to the AG, neither Mr. Stoller nor Mr. Lounsberry were able to justify the inclusion of a 2030 AMRP completion date as a condition to the requested merger.

The AG notes that its expert witness in this proceeding, Mr. Coppola, recommended scaling the pace and scope of AMRP activity to a level that, *inter alia*, targets high-priority and high-risk segments (AG Ex. 4.0 at 35:678-679), in light of evidence that PGL has not been historically tracking the risk level (known as the Main Rank Index) of each of its mains replaced (AG Ex. 4.0 at 9:138-10:162, 22:431-441). The AG suggests that this merger condition would address safety needs far more effectively than blithely instructing PGL to accelerate its AMRP to a timeline determined without any reference to safety considerations

6. The JA's Failure to Make a Meaningful Engagement With the AMRP's Significant Issues Will Lead to Adverse Rate Impacts for Peoples Gas's Customers.

The AG also argues that because of their failure to engage meaningfully – if at all – regarding the fate of the AMRP, the Joint Applicants failed to make the necessary showing under Section 7-204(b)(7) that the proposed reorganization will not have adverse retail rate impacts. such a showing. As described above, the AMRP has had – and will continue to have – severe adverse consequences on Peoples Gas's customers' bills. The AG observes that Peoples Gas has stated that the AMRP was the main driver for its need for increased rates in each of its last two rate increase requests. AG Ex. 4.0 at 17:324-326.

According to the AG, the record shows that the Joint Applicants' indifferent attitude regarding the AMRP may likely lead to even greater increases in program costs, and, therefore, rate increases, than those estimated by Mr. Coppola. The AG avers that the Joint Applicants' surprising lack of concern regarding the problem-plagued main replacement program includes the following failings:

- The Joint Applicants did not conduct a meaningful due diligence analysis of the AMRP.
- As admitted in their responses to the Commissioners' March 11, 2015 Data Requests, the Joint Applicants have not developed a transition plan for the AMRP. JA's Responses at 2.

● The JA do not know who will be responsible for managing the AMRP if the merger is approved. *See*, *e.g.*, *id.* at 3.

● In their March 11, 2015 Data Requests, the Commissioners asked whether any Peoples Gas or Integrys employees "with extensive AMRP management experience" would be retained. Commissioners' Data Requests at 2. The JA were unable to provide a direct response to the Commissioners' question, nor were they able to explain the process for evaluating whether PGL and Integrys employees currently overseeing the AMRP will be retained or replaced. Tr. at 214; JA's Responses at 2-3.

The AG states that these are a few examples of the seeming lack of interest the JA have displayed in the AMRP. The first two questions of the Commissioners' March 11, 2015 Data Requests sought information that they believed necessary "to ensure a seamless changeover that avoids any diminishment of the utility's ability to provide adequate, reliable, efficient, safe, and least-cost public service both leading up to and after closing the proposed reorganization, if approved." Notice of Commissioners' Data Request at 2. According to the AG, the Joint Applicants' failure to provide meaningful, direct answers to these questions should give the Commission significant pause.

The AG notes that in addition to the serious questions raised regarding whether the proposed merger meets the requirement of Section 7-204(b)(7) because of the JA's lack of focus on, and plans for, the AMRP, Staff witness Michael McNally conducted an analysis of the merger's potential impact on the Companies' cost of capital. The AG states that Mr. McNally testified that "[a]s a consequence of the proposed reorganization, the Gas Companies' credit ratings have been assigned a negative rating outlook from [Standard & Poor's]" (Staff Ex. 7.0 at 9:185-187) and that Mr. McNally explained that "[a]ll else equal, lower credit ratings would lead to higher debt costs, which in turn, would lead to higher equity costs as well, since higher debt costs increase financial risk." *Id.* at 10:217-219. The AG notes that although Mr. McNally proposed certain conditions to mitigate potential increases in the utilities' capital costs, he concluded that "it is not clear that the proposed reorganization will satisfy the requirement set forth in Section 7-204(b)(7) of the Act since it does not identify an acceptable means for eliminating any adverse rate impacts of the potential declines in the Gas Companies' credit ratings on their costs of capital." *Id.* at 17:392-395.

Finally, the AG pointed out that neither the JA nor Staff considered the impact of the JA's passive approach towards the AMRP in their respective assertions that the proposed transaction meets Section 7-204(b)(7)'s requirement that the Commission find that any proposed reorganization "is not likely to result in any adverse rate impacts on retail customers." The AG pointed out that Staff's Section 7-204(b)(7) analysis focuses solely on the impact the proposed merger would have on Peoples Gas's and North Shore's respective costs of capital. The Joint Applicants mention the potential impacts on the utilities' respective costs of capital as well as their agreement to not seek recovery of (1) any portion of the acquisition associated with the transaction and (2) the "transaction costs" incurred to accomplish the merger. The AG stated that whatever the merits of JA's and Staff's arguments on those points, neither party mentioned the flawed AMRP and the impact it will have on rates if the transaction were approved. The AG concluded that as much as the Joint Applicants may prefer to ignore the rate impacts of the AMRP, the Commission must account for adverse rate impacts the troubled program is likely to have on Peoples Gas's customers' bills if the proposed merger is approved.

The AG argues that in sum, the JA's remarkable lack of detail as to how they plan to conduct a seamless transition to managing the troubled AMRP and Mr. McNally's testimony regarding the proposed transaction's potential impact on the Companies' cost of capital demonstrate that the Joint Applicants have not proved that the proposed reorganization "is not likely to result in any adverse rate impacts for retail customers." 220 ILCS 5/7-204(b)(7).

7. Summary

In summary, the AG states that as Mr. Coppola stated in his Rebuttal testimony, a 20-year program at the time of the 2009 Rate Case “seemed like a reasonable timeframe,” but “now seems unrealistic and will likely cause further program cost overruns.” AG Ex. 4.0 at 33:643-645. The AG asserts that in light of the severe adverse rate impacts forecasted by Mr. Coppola (and undisputed by other parties), the absence of rate impact analyses from other parties, the lack of safety analysis associated with the date, PGL’s inability to date to manage the program on a 20-year timeline, PGL’s refusal to make an unequivocal commitment to the 2030 completion date without self-serving caveats, WEC’s lack of interest in doing necessary due diligence and formulating a seamless transition plan as to the AMRP’s problems, and Mr. McNally’s testimony regarding the proposed transaction’s potential impact on the Companies’ cost of capital, the Commission should reject the merger as proposed by the Joint Applicants, because such commitment would lead to rate shock for PGL’s customers, in clear violation of Section 7-204(b)(7) of the Act. The AG asserts that alternatively, if the Commission were to choose to approve the merger, it must reject the proposed 2030 completion condition.

B. Commission Analysis and Conclusion Regarding Section 7-204(b)(7)

Although this Commission directed Peoples Gas to complete the AMRP by 2030 as part of the Order in Docket Nos. 09-0166/0167 (cons.), that directive came in the context of the Commission’s simultaneous approval of Rider ICR. When Rider ICR was overturned by the Appellate Court in 2011, the directive to finish the AMRP on a 20-year time frame lost clarity, as the Commission indicated in its Order in Docket Nos. 12-0511/0512 (cons). The evidence advanced by AG witness Coppola shows that Peoples Gas is not now on a pace to complete the AMRP by the year 2030 – but that accelerating AMRP activities would, in fact, cause a significant increase retail customer rates, in violation of Section 7-204(b)(7) of the Act. Thus, before deciding whether Section 7-204(b)(1) is satisfied, the Commission decides as an initial matter that the proposal by Staff and by the Joint Applicants to include a re-commitment to a 2030 completion date as a condition of reorganization cannot be adopted.

Additionally, the Commission finds that the recent and significantly large rate increases for Peoples Gas customers would likely be worsened by a prospective takeover of PGL operations by Wisconsin Energy. The Commission finds that the limited analysis done by Staff and the JA – focusing primarily on the proposed transaction's effect on Peoples Gas's and North Shore's respective costs of capital – is insufficient. The tremendous costs and rate impacts of the AMRP require that the Commission consider whether the JA assumption of the main replacement program will "result will in adverse rate impacts on retail customers." The Commission finds that WEC's absence of any transition plans for the troubled AMRP suggest that it may allow cost overruns in the program to balloon beyond recent trends.

As described in more detail above, the evidence shows that the Joint Applicants did not meaningfully engage the past and ongoing problems with the AMRP. Evidence of the JA's failures are:

● The Joint Applicants did not conduct a meaningful due diligence analysis of the AMRP.

● As admitted in their responses to the Commissioners' March 11, 2015 Data Requests, the Joint Applicants have not developed a transition plan for the AMRP. JA's Responses at 2.

● The JA do not know who will be responsible for managing the AMRP if the merger is approved. *See*, *e.g.*, *id.* at 3.

In their March 11, 2015 Data Requests, the Commissioners asked whether any Peoples Gas or Integrys employees "with extensive AMRP management experience" would be retained.

Commissioners' Data Requests at 2. The JA were unable to provide a direct response to the Commissioners' question, nor were they able to explain the process for evaluating whether PGL and Integrys employees currently overseeing the AMRP will be retained or replaced. Tr. at 214; JA's Responses at 2-3.

The Commission is mindful of the AG's statement in their Initial Brief that the Commission cannot protect the interests of the utilities and their customers, as it is required to do under Sections 7-204, if it is investigating allegations of wrongdoing involving WEC and other members of the Joint Applicants in Docket No. 15-0186 while simultaneously moving ahead with a decision as to whether WEC should be permitted to acquire the Gas Companies in this docket. Moving forward to approve a merger under these circumstances is contrary to the ICC's obligation to protect the interests of utility customers. 220 ILCS 5/ 7-204(b),(f). Without having completed its investigation into the alleged wrongdoing, the Commission simply cannot be assured that the transition will not prolong or exacerbate dysfunction in PGL's AMRP. Indeed, the Commission has already asserted a connection between the merger and the investigation. Docket No. 15-0186, Corrected Initiating Order at 1.

Finally, Mr. McNally's largely unrebutted testimony suggests that the Joint Applicants have no plan to mitigate potential declines in the Gas Companies' cost of capital after the prospective merger.

Thus, the Commission finds that the showing required by Section 7-204(b)(7) has not been satisfied. The Commission agrees with the AG that the proposed transaction must be rejected because it does not meet Section 7-204(b)(1)'s requirement that it "is not likely to result in adverse rate impacts on retail customers." 220 ILCS 5/7-204(b)(7).

[IF THE COMMISSION REJECTS THE AG'S POSITION THAT THE PROPOSED TRANSACTION SHOULD BE REJECTED BECAUSE IT FAILS TO MEET SECTION 7-204(b)(7), THEN, AT A MINIMUM, THE COMMISSION SHOULD ADOPT THE CONDITIONS THAT WERE INCLUDED AS APPENDIX C TO THE AG'S INITIAL BRIEF.]

IV. If The Commission Approves The Merger, Several Conditions Under Section 7-204(f) Should Be Attached In Order To Protect The Public Interest.

A. AG's Position

The AG notes that the record evidence supports rejection of the Joint Applicants' assertions that the merger would not diminish the utility's ability "to provide adequate, reliable, efficient, safe, and least-cost public utility service" (220 ILCS 5/7-204(b)(1)) and that the proposed transaction "is not likely to result in any adverse rate impacts on retail customers." 220 ILCS 7-204(b)(7). In addition, the AG states that the Commission cannot protect the interests of the utilities and their customers, as it is required to do under Sections 7-204(b) and (f) of the Act, if it is investigating allegations of wrongdoing involving WEC and other members of the Joint Applicants in Docket No. 15-0186 but simultaneously moving ahead with a decision as to whether WEC should be permitted to acquire the Gas Companies in this docket.[24] Moving forward to approve a merger under these circumstances is contrary to the ICC's obligation to protect the interests of utility customers. 220 ILCS 5/ 7-204(b),(f). Without having completed its investigation into the alleged wrongdoing, the Commission simply cannot be assured that the transition will not prolong or exacerbate dysfunction in PGL's AMRP, according to the AG.

[24] In this instant proceeding, the AG, City, and CUB filed on March 24, 2015 a Motion for an Extension of the Schedule and Motion to Hold Open the Record for Additional Evidence in light of this new investigation and the receipt of new information in the JA's Responses to the Commissioners' Data Requests of March 11, 2015.

Indeed, the Commission has already asserted a connection between the merger and the investigation. Docket No. 15-0186, Corrected Initiating Order at 1.

Notwithstanding these procedural and evidentiary barriers to satisfying Section 7-204 requirements, should the Commission decide to approve a WEC/Integrys merger, the AG states that the record supports the addition of numerous conditions to help ensure the protection of the public interest pursuant to Section 7-204(f), which are summarized and attached as Appendix C to this Brief. As a starting point for the Commission's 7-204(f) analysis, it should be recognized that the list of commitments that the Joint Applicants have included as JA Ex. 15.1 REV as a condition of the merger are woefully insufficient to protect ratepayers and the public interest in general, as discussed below.

1. WEC's Proposed Commitments For Merger Approval Are of Little Tangible Value and Do Not Protect the Gas Companies' Customers.

The Joint Applicants assert that "the Reorganization is not one based upon synergies" and that if savings do occur, they "likely will not result from the Reorganization until after a 'ramp up' period of 5-10 years after the Reorganization closes." JA Ex. 2.0REV. (Lauber Revised Direct) at 12:251:260. In response, the AG states that the JA's claim that future benefits may arise from the reorganization is vague and offers no tangible value to PGL/NS customers. As described by City/CUB witness Gorman,

> The Joint Applicants have not identified any quantifiable ratepayer benefits. Their testimony on claimed ratepayer benefits describes possibilities and opportunities that may or may not yield benefits, years in the future. The described benefits are not specific, quantifiable, or useful as standards the utilities must meet.

City/CUB Ex. 4.0 at 247:566-569. As discussed further below, AG witness David Effron was similarly unimpressed, testifying that the merger should not be approved absent modifications to the employee headcount and rate commitments that would ensure any JA rate commitments are truly meaningful and beneficial to customers. AG Ex. 1.0 at 4:83-85. Each of the primary JA purported benefits is discussed below.

i. The JA's promise of future net savings as a result of the reorganization is so vague and unsupported as to be worthless.

In Direct testimony in this case, JA witness Reed claimed the reorganization "is likely to generate net savings in the range of three to five percent of non-fuel O&M of the combined company after a five to ten year ramp up period relative to what non-fuel O&M for the Companies would have been absent the transaction." JA Ex. 3.0 at 34:712-715. The JA, however, conducted no specific WEC/Integrys synergy savings analysis, the AG points out. Cross-examination revealed that of the 15 mergers Mr. Reed cited in support for his O&M savings estimates, 14 were based on savings *estimates* made before or at the cited merger closings. Tr. at 343. In other words, 14 of the 15 cited savings examples were merely unverified estimates, with no follow-up to see if the savings were achieved. Moreover, the one utility cited in Mr. Reed's sample that did provide an actual savings figure involved WEC's merger with a water company, according to the AG. Tr. at 343-344.

In the instant case, WEC is seeking a merger with a company (Integrys) that has already consolidated operations with another holding company, Peoples Energy Corporation, the former corporate parent of the Gas Companies, in 2007. The AG points out that that fact suggests any synergies that typically result from a merger of two holding companies will not necessarily produce any or comparable synergies when a similar holding company consolidation and reorganization has occurred within a relatively short time frame prior to the later merger. In the prior case, WPS Resource Corporation merged with Peoples Energy, as approved by the

Commission in 2007, and thereby creating the Integrys holding company.[25]. Mr. Reed admitted during cross-examination that Peoples Gas has likely already realized operational savings from the recent merger of its parent company with Wisconsin Public Service Corporation, the AG notes. Tr. at 344-345.

JAs further claim, generally, that the increased scale and scope of a reorganization will "create a financially stronger company with both greater financial liquidity and improved access to capital markets" (JA Ex. 3.0 28:576-577). But here again, the Joint Applicants did not describe any improved access to capital that does not already exist for the Gas Companies with their current parent, Integrys, the AG contends.

ii. The acquisition premium commitment is standard, and nothing more than business-as-usual merger treatment.

The Joint Applicants have committed to exclude the goodwill from the determination of the Gas Companies' rates, irrespective of whether push down accounting is required or not. The balance of goodwill on the Gas Companies' balance sheet, if any, will not be included in rate base. The JA further commit that amortization of goodwill, if any, will not be included in operating expenses. JA Ex. 1.0 at 22:471-474. In response to AG Data Request 2.02, the Joint Applicants have also represented that they will not include of any portion of the acquisition premium in common equity for revenue requirement purposes. AG Ex. 1.0 at 7:139-142. AG witness David Effron testified that these accounting treatments are appropriate and essential requirements of any reorganization involving a utility and are standard practice in merger proceedings. The Joint Applicants' commitment in this regard is therefore of limited value, at best, however, according to the AG's witness. AG Ex. 1.0 at 6-7:122-142. He explained that, as

[25] ICC Docket No. 06-0540, Order of February 7, 2007.

a general rule, goodwill is excluded from the determination of utility revenue requirements, as purchased goodwill does not represent an investment in assets used to provide utility service. *Id.* at 7:144-153. Therefore, it is unlikely that the goodwill would be reflected in the cost of service, even absent the Joint Applicants' commitment, the AG argues. *Id.*

iii. The JA's two-year rate freeze offer approximates PGL's current rate case filing timeline.

The Joint Applicants also committed to not seek increases in their base rates (just approved in January of this year) in ICC Docket Nos. 14-0224/0225 (cons.) "any earlier than two years after the Transaction closes." JA Ex. 1.0 at 21:454-455; JA Ex. 15.1 REV, par. 1. This commitment is heavily conditioned, as it is contingent on "the right to request that the Commission waive this base rate limitation if the financial integrity of Peoples Gas and/or North Shore is jeopardized to the extent of negatively affecting customers," the AG points out. *Id.* The evidence shows that this, too, has little tangible value to ratepayers, according to the AG.

During cross-examination, JA witness Leverett, who sponsored the JA's list of merger commitments, confirmed that a rate case could be filed by the Gas Companies 11 months prior to the two-year anniversary of the merger closing, or as early as August of 2016. Tr. at 169. It should be noted that the Gas Companies recently received a $71.1 million rate increase just two months ago.[26] Given that the Gas Companies have filed a rate case, on average, every 16.6 months since their 2007 rate case filing, this commitment does not suggest that the time period between the Companies' rate case filings would be extended significantly beyond a business-as-usual frequency, the AG points out.

[26] Order, Docket Nos. 14-0224/0225 (cons.), January 21, 2015; Second Amendatory Order, Docket Nos. 14-0224/0225 (cons.), February 11, 2015.

Moreover, the JA's rate freeze commitment falls short compared to the most recent Illinois-based natural gas utility reorganization commitment, that of AGL Resources in Docket No. 11-0046, the acquiring company of Nicor Gas, according to the AG. There, the AGL/Nicor Joint Applicants agreed to a *three-year* rate freeze as a merger commitment, *a full year longer than* what the JA in this docket promise. ICC Docket No. 11-0046, Order of December 11, 2011, Appendix A, condition no. 21. Here again, the AG states, the Joint Applicants' asserted benefits of the merger are underwhelming, at best.

iv. The JA's employee retention commitment is non-specific and is of no value.

As for WEC's promises to retain at least 1,953 full-time equivalent ("FTE") employment positions "in the State of Illinois for two years after the Reorganization closes," this, too, offers little value to customers, according to the AG. The commitment, while based on assumed FTE numbers for each Gas Company and Integrys Business Support, is made in the aggregate, not by company. AG Ex. 1.0 at 8:164-166. Further, as Mr. Effron notes, there is no description of how this commitment breaks down between administrative support and front line operational employees. *Id.* Moreover, in Direct testimony, Mr. Effron noted that in the recently completed PGL/NS rate case, Docket Nos. 14-0224/0225 (cons.), North Shore and Peoples Gas forecasted 178 and 1,356 FTEs, respectively, for the 2015 test year. *Id.* at 8:171-172. The JAs, in response to Mr. Effron's observation, asserted that these higher headcount numbers "represent the FTEs that will be needed to provide adequate, reliable, efficient, safe, and least-cost service in 2015 and 2016." JA Ex. 6.0 at 26:681-684. The JA added, however, that the 1,953 FTEs represent "a 'floor-level' of FTEs, below which the post-merger company, WEC Energy Group, will not allow its employment levels in Illinois to fall for a period of two years after the closing of the Transaction." *Id.* at 8-9:180-184.

In light of this information, Mr. Effron concluded that "[i]f, as claimed in the rate cases, the Gas Companies really expect to have 178 FTEs for North Shore and 1,356 FTEs for Peoples Gas in 2015, then the Joint Applicants' employee complement commitment in this case has little, if any substantive value, as there is little or no chance that the 'floor-levels' will ever be a factor in the Gas Companies' actual employee headcounts." *Id.* at 9:189-193. He noted that if the commitment to maintain designated employee headcounts is to have any value to customers and the Illinois communities the Gas Companies serve, "then further conditions must attach to this commitment." AG Ex. 3.0 at 3:56-65.

Thus, in order to provide any value to the WEC employee number commitment, Mr. Effron recommended that the Commission condition merger approval on the proper crediting to ratepayers of any savings due to the difference between the headcounts for the Test Year reflected in the revenue requirements presented by the Gas Companies in Docket Nos. 14-0224/14-0225 (cons.) and the Joint Applicants' employee headcount commitment in the present case. One option recommended by Mr. Effron would be to credit to customers the savings associated with a decreased employee complement post-merger, as compared to the FTE numbers PGL and NS forecasted in the rate case – a number that is reflected in current customer rates. Mr. Effron proposed that the differential in expense associated with these conflicting numbers be returned to PGL/NS customers by means of a rider that would commence at the closing of the Transaction and would continue until the rates in the Gas Companies' next base rate case go into effect. AG Ex. 1.0 at 20:437-444. The rider would be no different than any other merger commitment; it would exist because the JA had agreed to implement it to ensure that customers were not financially harmed by the merger, consistent with Section 7-204(b)(1) and (7) of the Act.

As AG witness Effron noted, the Joint Applicants' characterization of the minimum employee headcount commitment as a benefit to customers in the present case is inconsistent with the test-year employee headcounts presented by the Gas Companies in the rate cases as being necessary to provide safe and reliable service. Mr. Effron's rider credit proposal is an effort to give some substance to the Joint Applicants' minimum employee headcount commitment, on a *forward looking* basis. While the Joint Applicants and Staff complained that the ratemaking prohibition against single-issue ratemaking is triggered by the proposal, it is in fact an effort to resolve the inconsistency that PGL and NS created by forecasting higher FTE numbers in the rate case (thereby maximizing revenues) and the JA's commitment in this docket to a lower combined FTE number post-merger – a number that the JA admit is lower than the FTE amount that "will be needed to provide adequate, reliable, efficient, safe, and least-cost service in 2015 and 2016." JA Ex. 6.0 at 26:681-684. Importantly, it demonstrates that this JA commitment neither ensures the maintenance of existing service quality nor least cost rates, according to the AG. The bottom line is that if the Commission is to believe Mr. Leverett's claim that the higher rate case forecasted FTE numbers are needed "to provide adequate, reliable, efficient, safe, and least-cost service in 2015 and 2016," then the JA's commitment to retain a lower number as the FTE "floor" is of no benefit to customers, and potentially evidence of a planned degradation of service quality. AG Ex. 3.0 at 4:76-87.

The AG argues that Mr. Effron's proposal (or a modification of that proposal that captures this revenue difference) should be adopted as a condition of any Commission merger approval, pursuant to Section 7-204(f), as discussed below.

v. The JA proposed no service quality improvements.

WEC appears to have made no investigation or attempt to remedy service quality issues at the Gas Companies, the AG points out. In fact, problems with PGL field work, customer interaction and prompt establishment of natural gas delivery service were documented as recently as PGL's last rate case, ICC Docket Nos. 14-0224/0225 (cons.), according to the AG. *See* AG Ex. 5.0, AG Ex. 6.0, *gen'ly*. This disinterest in service quality issues as a proposed merger benefit is unrebutted, as revealed in cross-examination of JA witness Leverett:

> **REQUEST NO. 2.29:** Are the Joint Applicants proposing any specific, enforceable quality of service improvements as a part of the reorganization?
>
> **RESPONSE:** At this time, the Joint Applicants have not proposed any quality of service improvements as a part of the proposed Reorganization.

CUB Cross Ex. 1. This evidence speaks for itself, according to the AG. The merger will not result in any utility service benefits for PGL/NS customers, the AG concludes.

vi. The JA's commitment to implement the Liberty final report audit recommendations is heavily conditioned and omits any reference to implementation of Liberty Interim Report recommendations.

The fact that the JA have no transition plan for assuming ownership of Peoples Gas and oversight of the very troubled AMRP is made worse by the fact that the Joint Applicants' commitment to implement the Liberty audit report recommendations is limited to the *final* report – not the Interim Report as well, according to the AG. On cross-examination, JA witness Giesler (the Integrys employee with management responsibilities over significant portions of the AMRP) testified that there is a process that is developing plans to implement a "series of changes" that the senior management of Peoples Gas and Integrys and the Liberty auditors agree need to be implemented before the beginning of the next construction season. Tr. at 273. But the JA have not committed to continuing those ongoing, curative activities. Tr. at 148, 200-201.

The AG states that even the JA's commitment to implement the final audit recommendations is a heavily conditioned one. As AG witness Coppola noted, the Supplemental Rebuttal Testimony filed by both WEC witnesses Leverett and Hesselbach does not make a convincing case that the Joint Applicants have fully embraced the recommendations contained in the Interim Report. AG Ex. 6.0 at 2-3:29-46. Conspicuously absent from the Joint Applicants' evidentiary presentation was any testimony from the companies now operating and in charge of the AMRP – Peoples Gas and its parent company, Integrys according to the AG. The absence of any testimony by Integrys and Peoples Gas addressing (i) the findings and recommendations contained in the Interim Report, and (ii) how they would ensure that their new corporate parent continues any progress made to date, leaves a significant void in this evidentiary record, the AG argues. This lack of commitment to ensure a smooth transition between now and the time that WEC receives a Commission decision or closes on the Reorganization will likely have a detrimental impact on the operation, safety, and rates of Peoples Gas, according to the AG. AG Ex. 6.0 at 5-6:96-100.

Thus, the JA's conditioned commitment to implement only the Liberty *final* audit recommendations does not ensure that the reorganization will not diminish safety, reliability and the cost of utility service, the AG reasons. 220 ILCS 5/7-204(b)(1), (7). In fact, the AG points out that WEC's commitment to implement final Liberty audit recommendations are already required for Peoples Gas under the Commission's 2012 Rate Case Order. The Commission's order made clear that Peoples Gas would be required to implement audit recommendations without condition. The Commission stated:

> For reasons detailed in Staff witness Buxton's rebuttal testimony (Staff Ex. 20.0 at 23-24) and immediately above, this Commission adopts Staff's proposed two-phase investigation of the AMRP under Section 8-102 of the Act (220 ILCS 5/8-102) ending in a public document report. This Order directs Staff to conduct the tasks outlined on pages 3-8 of Staff Ex. 20.0 and directs Peoples to comply with the same.

ICC Docket Nos. 12-0511/0512 (cons.), Order of June 18, 2013 at 61. Mr. Buxton's testimony required the following of PGL:

> The Commission's consulting contract should include two phases. Phase I will be the investigation. *Phase II will be a two-year verification period following the Phase I investigation and the engineering consultant who performs the investigation should work during this Phase II two-year period to verify that Peoples has implemented the recommendations from the Phase I investigation.*

ICC Docket Nos. 12-0511/0512 (cons.) at 61, citing Staff Ex. 20.0 at 3-4 (emphasis added). Thus, the AG asserts, PGL is already required, per Commission order, to implement audit recommendations – and not in any kind of conditioned format, as the JA's commitment numbers 9 through 11 are, as discussed above.

vii. Other WEC commitments are already required of PGL pursuant to law and/or Commission order.

The JA have committed to establish a new training center within the City of Chicago, the extension of funding of technical training for future gas utility workers at Chicago's City Colleges (JA Ex. 15.1 REV, nos. 37 and 38), and to contribute $5 million over five years to the Gas Companies' Share the Warmth Fund. While the People appreciate these commitments, the promises are insufficient in light of the risks of rate shock associated with the JA's rudderless assumption of the AMRP. WEC's other proposed merger commitments offer little or no tangible value and amount to no more than what the Gas Companies are already required to do under Commission order or statute, the AG asserts.

In addition, the AG states, filing requirements for both the JA-proposed AMRP activity and other merger-related monitoring and ratemaking activities represent standard, boiler-plate filing requirements that are necessary but unremarkable in scope. *See, e.g.,* JA Ex. 15.1 REV, commitment nos. 3, 4, 6, 7, 8, 9-13, 16, 17-25. These commitments represent business-as-usual activity that is either already happening under Integrys's leadership or is standard practice when acquisitions are approved by the Commission.

In sum, other than technical employee training funding and the Share the Warmth contributions, the JA commitments promise little, if any tangible benefits for PGL and NS customers, according to the AG. This was perhaps best signified in the JA's Direct testimony presentation that promised that "[c]ustomers will continue to receive high-quality, adequate, safe, and reliable gas service just as they did before the Reorganization, and…at the same cost as they would have absent the Reorganization," notwithstanding the barrage of rate increases PGL customers have experienced since 2008, along with the well-documented mismanagement of the AMRP. JA Ex. 1.0 at 16:350-353. Coupled with their failure to create a transition plan for the AMRP and blind commitment to its troubled trajectory, the Joint Applicants' "commitments" will result in a deterioration of service and rate shock, as noted earlier in this Brief, and do not protect the public interest, according to the AG.

2. The AG-Proposed Conditions Will Help Ensure Protection of the Public Interest, Consistent with Section 7-204(f) of the Act.

The AG argues that the Commission must ensure that the interests of the Gas Companies' customers are protected. The AG points out that Section 7-204(f) of the Act permits the Commission to condition any merger approval to ensure that such approval would not result in increased rates and diminished safety and reliability in the Gas Companies' utility service in order to protect the interests of the Gas Companies' customers. 220 ILCS 5/7-204(f). The AG recommends the Commission adopts several minimum conditions, should the Commission approve the merger, discussed below.

i. The Joint Applicants should be required to commit to reassessing the completion timeline of the AMRP.

The AG argues that the Commission must not blindly adopt the Joint Applicant's commitment to complete the AMRP by 2030 – a date that the record and this Brief make clear has no validity in terms of safety assessment or law. To do so would not ensure the safety and reliability of the PGL delivery system and lead to rate shock, according to the AG.

As AG witness Coppola and City witness Cheaks testified, Peoples Gas has been unable to maintain a pace that would allow them to complete the AMRP by 2030. That fact is unrebutted, the AG points out. Even the Company's current pace has resulted in huge cost overruns and unrelenting rate increases since the AMRP was approved in 2010. Mr. Coppola's assessment of the rate impacts of blindly attempting to maintain an arbitrary 2030 completion date makes clear that the Commission must require the Joint Applicants to commit to improving the current operation of the AMRP by reassessing the scale and timeline of the program to a manageable level, the AG states. In addition, the AG states that the Joint Applicants must be required to commit to implementing *all* findings – both Interim and Final – of the Commission-ordered Liberty audit now being conducted. With that in mind, any approval of the merger should be conditioned on the JAs committing to the following AMRP improvements, according to the AG:

i. Peoples Gas shall perform a thorough evaluation of the AMRP and scale the program to a level of cast iron/ductile iron replacement and related infrastructure upgrades that is manageable, targets high priority, high risk segments first, cost- effective, and minimizes the impact on customer rates.

ii. Peoples Gas shall commit to a transparent process of providing annual reports to the Commission, reconciling its actual vs. forecasted AMRP investments, and provide an accounting of financial and non-financial benefits realized from the AMRP to date.

iii. Peoples Gas will present to the Commission an annual, detailed, work plan for the remainder of the AMRP program that shows: (1) the planned infrastructure replacement segments for the upcoming 12-month period and their related cost; (2) the Main Ranking Index ("MRI") of each planned targeted segment; (3) a list of the mains and other infrastructure that are still in need of replacement, along with their respective MRI ranking and projected cost to complete; (4) the total projected annual cost to complete the program and quantity of mains, services, meters and other infrastructure to be replaced and installed. (5) an explanation and detailed corrective action/implementation plan for improved coordination with the City of Chicago permit and public works activities; and (6) a detailed corrective action plan and status report for implementation of the approved final recommendations from the pending outside audit.

iv. Peoples Gas shall credit customers for all construction fines and penalties paid from the beginning of 2011 to date to the City of Chicago, plus any fines and penalties incurred through the close of the merger, that were recovered in base rates or infrastructure riders. The credits could be flowed through PGL's Rider QIP during a single month or alternatively contributed by PGL to its "Share the Warmth" fund.

v. Going forward, Peoples Gas shareholders should bear the costs of any such City of Chicago fines and penalties associated with AMRP and other construction activity.

vi. The Joint Applicants shall commit unconditionally to implement all audit recommendations of *both* the Interim and Final Liberty audit reports.

vii. The Joint Applicants shall commit to fully cooperating with the Commission's investigation into allegations of misconduct and improprieties in the PGL AMRP (ICC Docket No. 15-0142), and implementing any corrective actions, including customer refunds of AMRP costs deemed imprudent by the Commission, as ordered by the Commission in that and any other docket related to review of the AMRP and PGL's Rider QIP. (AG Ex. 3.0 at 6.0 at 2-3:37-46.)

viii. The Joint Applicants shall commit to City of Chicago witness Cheaks' proposed conditions that are designed to revamp PGL's coordination with CDOT. They include:

- Requiring a weekly, block-by-block schedule of construction activities be given to CDOT and the ICC, provided on a five-year, annual, and monthly basis.
- Requiring that any Field Order Authorizations or Change Orders be communicated within 24 hours to CDOT.
- Requiring the newly formed entity to actively participate in CDOT's dotMaps website in order to better collaborate with all occupants of the Public Way.
- Requiring that PGL improve their performance in the following categories, with financial penalties for failure to improve that cannot be recovered from PGL's ratepayers:
    - Permitted timeframe adherence (being on schedule more often)
    - Approved capital and O&M spend adherence (being on budget more often)
    - Change order spending and communication
    - Management reserve spending and budgeting
    - Time needed to close Field Order Authorizations and Change Orders
    - Contractor "Hits" on City facilities (City/CUB Ex. 3.0 at 4-5.)

These conditions will help to ensure both the safety and reliability of the Peoples Gas distribution network and that the impact of the AMRP on future customer rates will be minimized, thereby ensuring least cost utility service in accordance with Sections 7-204(b)(1) and (b)(7), according to the AG.

ii. The Joint Applicants should be ordered to freeze rates for five years.

Particularly in light of the Gas Company's revenue stabilizing mechanisms, the AG argues that the JAs should be required to adopt a five-year rate freeze as a condition of the merger. As observed by City of Chicago/CUB witness Michael Gorman, Section 9-220.3 of the Act authorizes some Illinois gas utilities, including PGL, to file a tariff for a surcharge that adjusts rates and charges to provide for recovery of costs associated with QIP investments. City/CUB Ex. 4.0 at 3:73-76. PGL currently uses this rate mechanism to earn a return of and on its investment in the AMRP throughout the year and between rate case filings. The qualifying QIP capital investment is more than 70% of the total capital investments Integrys management plans over the next five years. JA Ex. 1.0 at 18. The QIP surcharge, approved on January 7, 2014, in ICC Docket No. 13-0534, allows PGL to recover a return of and on investments for: (1) the costs to install facilities to retire cost iron/ductile iron gas distribution facilities; (2) gas meter relocation costs to move meters from inside customers' premises to outside; (3) the cost of upgrading the gas distribution system from a low pressure system to a medium pressure system, including installation of high-pressure facilities to support the upgrade; (4) the cost to replace high–pressure transmission pipelines identified as at higher risk of failure; and (5) the cost to install regulator stations to establish over-pressure protection, the AG points out. City/CUB Ex. 4.0 at 24:87-95.

City/CUB witness Gorman stated that this rider mechanism is a significant revenue stability mechanism for the Gas Companies that was of particular interest to WEC investors. The AG points out that WEC noted in a November 2014 investor presentation that the Rider QIP surcharge will provide "Immediate earnings as infrastructure investments are made (return on and of capital costs)." *Id.* at 4:104-105. PGL's QIP rider mechanism for assured recovery of and on PGL's increasing rate base (due to AMRP) is a major element of the utility's premium value to the acquiring firm, WEC, Mr. Gorman noted. *Id.*

Mr. Gorman also testified that in a report on Integrys, *Value Line* stated that the existence of new regulatory mechanisms in Illinois will allow PGL to support earnings growth without filing rate increases, even as it pursues its large AMRP capital program. He noted, too, that Rider QIP was not available during the acquisition of Nicor Gas by AGL. Thus, this rider increases PGL's revenue stability as compared to that of Nicor, and yet, as noted above, AGL agreed to freeze Nicor rates for three-years post-merger as a condition of its reorganization approval, according to the AG. Mr. Gorman further noted the fact that in its November 2014 presentation to investors, Integrys highlighted several innovative ratemaking mechanisms that reduce its risks, including Rider QIP, the Gas Companies' uncollectibles rider, storage service rider, implementation of a permanent decoupling mechanism in 2012, and the existence of a rider to recover manufactured gas plant site cleaning cost. *Id.* at 5:124-129. Mr. Gorman noted that while these revenue stability mechanisms significantly reduce the JA's revenue-recovery risk, and increase the market value of Integrys and the Gas Companies, they result in increased rate instability for customers.

Like AG witness Effron, Mr. Gorman was unimpressed with the JA's offer of a two-year rate freeze as a merger commitment, the AG points out. *Id.* at 8:179-182. He recommended, and the AG supports, implementation of a five-year rate freeze should the merger be approved. There is substantial evidence in the record that this commitment is justified given the Gas Companies' revenue stability mechanisms and the investor community's acknowledgement and recognition of the revenue recovery mechanisms, according to the AG. In addition, since the initiation of this docket, the Illinois Supreme Court affirmed the Commission's approval of the permanent decoupling mechanism, thereby settling any uncertainty associated with the fate of the decoupling rider and its ability to reduce revenue recovery risk for the Gas Companies. *People of the State of Illinois ex rel. Lisa Madigan vs. Illinois Commerce Commission*, 2015 IL 116005, January 23, 2015 (the "Supreme Court Decoupling Opinion").

Without protective actions by the Commission, Mr. Gorman testified, that added value could flow to the acquiring company's shareholders, rather than enhancing the utilities' ability to provide safe, reliable infrastructure and adequate, least-cost service. He concluded that with all these riders in effect, the Joint Applicants should be able to defer an increase in base rates for a longer time period, particularly given that he projects more than 70% of PGL's planned capital expenditures will be subject to recovery through Rider QIP, and that the existence of the rider should help provide sufficient funding for PGL and NS to make qualifying capital investments during the base rate freeze period. Mr. Gorman concluded that "a longer term base rate freeze period will provide customers some assurance of benefits from the reorganization." *Id.* at 10:230-232.

In addition, Mr. Gorman noted that a financial integrity provision to the rate freeze commitment is not necessary, but if included, should clarify that any rate freeze waiver for financial integrity needs must meet a high standard, and should be based on the necessity of an increase in rates, such as being necessary to maintain an investment grade bond rating outlook, and not on a "mere expectation that PGL and NS earnings may be reduced." *Id.* at City/CUB Ex. 4.0 at 10:242-243.

In response to the City/CUB proposed five-year rate freeze merger commitment proposal, the JA again argue that this proceeding "is not to create benefits or other enhancments in a utility's service quality before approving a reorganization" [sic]. JA IB at 44. In the JA's view of the case, if the Commission concludes that the required findings under subsection (b) of the statute that the proposed merger "will at least maintain the utility's status quo and not diminish or adversely impact the utility's service quality or rates" the merger must be approved. *Id.*

Again, as noted repeatedly above, this interpretation of the Commission's obligations under Section 7-204 of the Act is simply wrong, and would render subsection (f) of the statute meaningless, according to the AG. That viewpoint runs counter to well-established rules of statutory interpretation.

The JA also argue that the proposal does not take into account the 5.5% annual cap included in Rider QIP or that City of Chicago regulations "have led to dramatic increases in the costs of performing operational work" that will not be recovered in either the Rider or the 2014 rate case, citing JA witness Leverett's Rebuttal testimony. JA IB at 45. These arguments, too, should be rejected, the AG states. A review of the cited testimony that proffers these arguments (JA Ex. 6.0 at 34) includes no specific discussion of dollar amounts tied to either the Rider QIP claim or the amount of extraordinary expenses incurred as a result of the new City regulations. Moreover, given Mr. Leverett's astounding lack of knowledge about either the AMRP or Rider QIP revealed in cross-examination, these arguments ring hollow. *See, e.g.,* Tr. at 146-237.

In addition, the Joint Applicants suggest that rather than committing to a rate freeze, net savings will occur over time, citing the testimony of JA witness Mr. Reed. JA IB at 45. But Mr. Reed's claimed savings were so vague as to be meaningless, and his comparison of savings that occurred in other mergers proved to be irrelevant to the instant proceeding, the AG points out. *See* AG Initial Brief at 49-50; Tr. at 343-345.

The AG states that there is substantial evidence in the record that this commitment is justified given the Gas Companies' revenue stability mechanisms and the investor community's acknowledgement and recognition of the Gas Companies' revenue recovery mechanisms, as noted by City/CUB witness Gorman. *See* City/CUB Ex. 4.0 at 10. In addition, since the initiation of this docket, the Illinois Supreme Court affirmed the Commission's approval of the permanent decoupling mechanism known as Rider VBA, thereby settling any uncertainty associated with the fate of the decoupling rider and its ability to reduce revenue recovery risk for the Gas Companies. *People of the State of Illinois ex rel. Lisa Madigan vs. Illinois Commerce Commission*, 2015 IL 116005, January 23, 2015 (the "Supreme Court Decoupling Opinion"). As City/CUB witness Gorman testified, without protective actions by the Commission, that added value could flow to the acquiring company's shareholders, rather than enhancing the utilities' ability to provide safe, reliable infrastructure and adequate, least-cost service. His conclusion that "a longer term base rate freeze period will provide customers some assurance of benefits from the reorganization" is supported by the record. City/CUB Ex. 4.0 at 10:230-232.

In sum, the AG urges the Commission to adopt Mr. Gorman's five-year rate freeze commitment recommendation as a condition of merger approval.

iii. The JA should be required to cap residential revenue recovery through fixed charges to 40%.

It is no secret that in addition to experiencing the financial pains of five PGL/NS rate increases over the last seven years, the Gas Companies' customers have seen their fixed monthly customer charges grow to 63% of the bill for PGL customers and 73% for NS customers. Peoples Gas and North Shore Gas customers now pay the highest fixed monthly customer charges and overall rates in Illinois, with customer charges at $30.84 and $23.94 for Peoples Gas and North Shore heating customers, and $16.37 and $15.70 for Peoples and North Shore non-heating customers, respectively, the AG points out.[27]

Including a merger condition that lowers the customer charge portion of the bill such that no more than 40% of revenues is collected through the residential heating class customer charge is in the public interest and fully justified if customers are to see value from the reorganization beyond any rate freeze commitment, according to the AG. Adding the customer charge cap to the merger condition list is particularly appropriate in view of facts arising since the filing of testimony in this case and the Commission's January 21, 2015 rate case Order in Docket Nos. 14-0224/0225 (cons.): specifically, the January 23, 2015 Supreme Court Decoupling Opinion, which affirmed the Commission's approval of Rider VBA (Volume Balancing Adjustment)[28]. Since the Supreme Court's decision now guarantees that Peoples Gas and North Shore Gas will continue to recover their entire Commission-approved revenue requirement each year, the AG argues that the Commission should add the customer charge reduction commitment to the list of merger conditions in light of the increased value this reduction in shareholder risk brings to WEC.

The Supreme Court's decision just two days after entry of the Commission's Final Order in Docket Nos. 14-0224/0225 (cons.) provides added value to WEC shareholders because it effectively settled any uncertainty as to whether the Gas Companies would be permitted to retain

[27] http://www.peoplesgasdelivery.com/company/tariffs/sc1.pdf; http://www.northshoregasdelivery.com/company/tariffs/sc1.pdf (last accessed March 27, 2015).

[28] Rider VBA uncouples the Companies' revenues from their sales such that utilities that have "decoupling" riders have recovery of the full amount of their Commission-approved revenue requirement guaranteed, through an annual reconciliation process that accounts for under-recovery or over-recovery of approved revenues and authorizes customer bill surcharges or credits, respectively. The Commission first approved a pilot for Rider VBA in its 2007 rate case proceeding, Docket Nos. 07-0241/07-0242 (cons.). After the four-year pilot ended, the Commission approved Rider VBA on a permanent basis in its January 10, 2012 decision in Docket Nos. 11-0280/11-0281 (cons.).

their decoupling riders going forward, according to the AG. A WEC commitment to lower the customer charge to a level that caps recovery of revenues through the fixed charge portion of monthly customer bills would acknowledge this reduction in risk and provide a tangible value to PGL/NS customers. Doing so, too, would provide Peoples Gas and North Shore customers more control over their natural gas bills, enabling the General Assembly's public policy goal of reducing the usage of natural gas and achieving least cost utility service, consistent with Sections 8-104 and 1-102 of the Act, the AG states. In addition to providing some tangible benefit to the Gas Companies' customers, the AG notes that lower customer charges minimize cross-subsidies of high users by low users of natural gas, and serves the General Assembly's and the Commission's goal of encouraging energy efficiency by giving customers more control over their bills

In view of these new facts and circumstances regarding Rider VBA and the revenue protections it now offers the Joint Applicants on a permanent basis, and in light of the fact that ratepayers have seen their monthly customer charges rise by almost 200% (Peoples) and 179% (North Shore) since the inception of Rider VBA, the AG urges the Commission to condition merger approval on a (revenue-neutral) lowering of the customer charge that would provide additional, tangible value to the Gas Companies' customers outside of any rate freeze condition, and is consistent with the public interest.

iv. Any merger approval should include a dividend ring-fencing provision.

The AG supports City/CUB witness Gorman's recommendation that should the Commission approve the merger, a dividend ring-fencing provision should be a requirement of the approved reorganization. The AG states that City/CUB witness Gorman testified that after any Commission-approved Integrys/Gas Companies acquisition, WEC still will need to draw sufficient cash from its subsidiaries (including PGL/NS) to pay dividends to WEC public shareholders, and to pay its debt. City/CUB Ex. 4.0 at 14:333-336. In response to City Data Request 6.01, the Joint Applicants provided the financial forecast that it also provided to credit rating agencies, which was used to assess the credit metric impact on the Joint Applicant utility companies and WEC after the merger. *Id.* at 14:340-343. In that forecast, Mr. Gorman testified, the consolidated operations are projected to produce enough cash flow to support the additional $1.5 billion of acquisition-related debt. However, if WEC requires its utilities to pay higher dividends, "the cash flow available to utilities for making system modernization will be reduced, and that could either delay replacement of aging infrastructure, or require the utilities to rely more on external debt." *Id.* at 15:348-351. A need for more external debt could increase the financial leverage of the utilities, erode their credit standing, and harm the utilities' ratepayers, either through diminished service or higher costs of service in rates, Mr. Gorman testified. *Id.* at 15:348-359.

In order to evaluate the likelihood of increased demands on the Gas Companies to pay dividends to WEC, Mr. Gorman conducted an assessment of whether or not the projected level of dividend payments from utility companies up to WEC is able to support both public dividend payments and the acquisition debt service. He performed this analysis by comparing the forecasted level of utility dividend payments up to WEC, with the amount of cash WEC needs to pay its public dividends and to service the $1.5 billion of acquisition-related debt, as outlined in confidential City/CUB Exhibit 4.1. The AG notes that he concluded that "WEC's planned public dividend payments from utility subsidiaries up to WEC may not be adequate both to pay the forecasted public dividend payments and to service the acquisition debt based on the 15-year amortization schedule" and that "the proposed Transaction will create some incentive for WEC to maximize the cash withdrawal from its utility subsidiaries in order to service the significant increase in debt at the parent company level, and to pay its public dividends." *Id.* at 16: 381-384. Mr. Gorman noted that "[d]ividend payments to WEC from a utility will reduce the amount of internal funds that remain in the utility and that are available to fund utility infrastructure investments. As such, if WEC requires the utility to increase the amount of dividend payments up to WEC so it can service its own public dividends and acquisition-related debt, then the amount of internal cash available to the utilities to support their own capital investment programs will be reduced." *Id.* at 16-17:390-395.

The AG points out that Mr. Gorman testified that "the amount of dividends utilities would be expected to pay up to WEC to enable the parent to meet its public dividend payments, and its other financial obligations is a factor the Commission must consider in determining whether the reorganization can be or should be approved." *Id.* at 17:400-404. Importantly, Mr. Gorman testified that WEC's own projections suggest an increase in the percentage of utility earnings paid out as dividends to WEC over the forecast period, compared to before the merger. *Id.* at 17:408-409. In total, WEC's projections show that utility subsidiaries pay out 89% of utility earnings up to WEC as dividend payments and that, aside from the ratepayer funds collected through PGL's infrastructure rider QIP, only a reduced fraction of PGL's retained earnings or new debt (with consequences noted earlier) will be available to support PGL's AMRP. *Id.*

Mr. Gorman further noted that Standard & Poor's, Moody's and Fitch have all noted the increased financial obligation being taken on by WEC as a result of the acquisition, and recognize "that WEC's only source of cash will be its utility subsidiaries," according to the AG *Id.* at 18:432. Importantly, because the Wisconsin utility subsidiaries have regulatory insulation that limits the amount of dividends that the utilities can pay to WEC in order to satisfy this acquisition debt obligation, Mr. Gorman testified that the Wisconsin PUC's ratepayer protections and service quality in that state "will undoubtedly result in pressure to increase the amount of cash withdrawn from non-Wisconsin utilities as a result of the acquisition." *Id.* at 18: 436-438.

Indeed, the AG points out that Supplemental Direct testimony of JA witness Scott Lauber indicated that WEC's debt will increase from $817 million at year-end 2013, up to $2.3 billion by year-end 2015. JA Ex. 5.0 at 6:107-114. He states that this level of debt will increase from 15.6% of consolidated debt at year-end 2013 up to 20.8% of consolidated debt by year-end 2015, and that the amount of acquisition debt included at the parent company level will result in parent company debt equal to approximately 31.3% of total consolidated company debt at year-end 2015. *Id.* at 6-7:120-135. Mr. Gorman noted that "[b]y any reasonable measure, the proposed financing structure will significantly increase the amount of debt at the parent company level," thereby increasing dependence on cash flows from the utilities. *Id.* at 20-21:494-496. Mr. Gorman concluded that "there is a near-certainty that this planned level of parent company debt will increase the utility companies' dividend payment obligations (as the Joint Applicants themselves forecast)" and potentially restrict the amount of internal cash flow available to the utility companies to support utility capital investments. *Id.* at 21:500-504.

While the Joint Applicants reject the need for any "ring-fence" protections to ensure that the Gas Companies are able to fund their planned capital improvements before sending money up to the corporate parent for shareholder dividend payments, City/CUB witness Gorman viewed them as essential. The People agree and support this as a necessary condition to merger approval to protect the interests of both of the Gas Companies, particularly PGL, given its AMRP commitment in the City of Chicago.

v. AG witness Effron's proposal to reflect the Joint Applicants' most recent forecast of Integrys Customer Experience project savings in rates should be included among merger conditions.

The AG asserts that merger approval should also be conditioned on the JA's agreement to provide an additional rate benefit to PGL/NS customers based on new information in the record in this docket that demonstrates that the Gas Companies will be experiencing significant savings post-merger related to ratepayer financing of the Integrys Customer Experience ("ICE") project.[29]

However, the Gas Companies have taken contradictory positions in the 2014 rate case and this proceeding as to whether savings associated with the ICE project will be realized sooner than forecasted in the rate case, the AG points out. In particular, the Gas Companies included $9.2 million in expenses associated with the ICE project in their revenue requirements in Docket Nos. 14-0224/14-0225 (cons.); asserted that the ICE system would result in significant efficiencies that will produce cost reductions; and did not reflect savings associated with the project in the 2015 test year. But then, in discovery responses in this docket from the Joint Applicants, they provided updated information that showed ICE project estimated net benefits beginning in 2015. AG Ex. 1.0 at 14-16:309-363. In fact, Mr. Effron testified, it is expected that ICE will produce a " 'net benefit (a credit to expense, i.e. pre-tax reduction in O&M),' " which is " 'derived from forecasted system savings greater than forecasted system costs' " *Id.* at 13-14:298-301, citing Joint Applicants' response to Data Request AG 2.13, attached as AG Ex. 1.3.

[29] The ICE project will unify Cfirst, which is the customer information system that Peoples Gas [and North Shore] currently uses, and the various customer information systems currently in use across Integrys. It will provide significant benefits to Peoples Gas [and North Shore] and the other Integrys regulated utilities such as improved efficiency and productivity and standardization of internal delivery which will improve customer satisfaction. In addition to unifying systems, the ICE project will improve and enhance billing, collections, call center, and self-service related offerings by ensuring that these functions are staffed appropriately to continue to leverage the opportunities of a large corporation, while maintaining the high level of service of a local utility. AG Ex. 1.0 at 12:269-284 (citing Docket Nos. 14-0224/14-0225 (cons.), PGL Ex. 13.0, at 10:207-215 (bracketed text added)).

This new information provided in this case contradicted the Gas Companies' position in the 14-0224/0225 rate case that ICE savings would not be achieved until 2016, with no reductions in the 2015 Test Year. *Id.* at 14:309-311. Response to AG Data Request PGL 11.08, Docket Nos. 14-0224/14-0225 (cons.), attached as AG Ex. 1.4. In other words, Mr. Effron testified, "based on the scenario presented by the Gas Companies in the rate cases, the in-service of the ICE project would be precisely timed so that a full year of costs (in excess of $19 million) would be billed to the Gas Companies in the twelve-month period that just happened to coincide with the Test Year, while, conveniently, no savings whatsoever (savings that would fully offset those costs) would be experienced until one day after the end of the Test Year." *Id.* at 14:312-318. He characterized this timeline assessment as "improbable in the extreme." *Id.* at 14:317-318.

The Joint Applicants asserted that the basic justification for these inconsistencies was "that the response to AG 3.05 was support for an item in Joint Applicants' Ex. 4.1 and that data underlying Ex. 4.1 were from the long-term financial forecast. The rate case data in the Gas Companies' Docket Nos. 14-0224/14-0225 (cons.) are to support a forecasted 2015 Test Year. The documents will necessarily be inconsistent because they were prepared at different points in time." *Id.* at 17:366-372. But Mr. Effron noted that when the AG asked the Joint Applicants (in AG Data Request 3.06, attached as AG Ex. 1.7 to describe revisions, identify when the revisions took place, and quantify the effect of the revisions on the forecasted year-by-year costs and benefits of the ICE project, the Joint Applicants described one, and only one, change: "*Subsequent to the compilation of data underlying JA AG 3.05 Attach 01 CONFIDENTIAL, the estimated ICE implementation date for the Gas Companies has moved from the second to the third quarter of 2015.*" *Id.* at 17:382-385.

In response, Mr. Effron observed:

> …if the estimated ICE implementation date for the Gas Companies was moved *back* from the second to the third quarter of 2015, it seems illogical that the billing for the ROA/depreciation on the ICE project would be moved *forward* from the beginning of 2016 to the beginning of 2015, as was assumed by the Gas Companies in the rate cases. And there is no way that moving the ICE implementation from the second to the third quarter of 2015 can even begin to explain the $10 million discrepancy between the 2015 ICE O&M expense allocated to the Gas Companies in JA AG 3.05 Attach 01CONFIDENTIAL and the 2015 ICE O&M expense allocated to the Gas Companies in the rate cases.

Id. at 17-18:386-394.

Accordingly, the evidence in this case shows that if there is no adjustment to the ICE costs forecasted by the Gas Companies in those cases, the Gas Companies will be recovering $19.2 million in non-existent expenses when the ICE project goes into service. *Id.* at 18-19:409-414. In effect, during the term of the proposed rate freeze, the customers would be charged for all of the annual costs of the ICE project, while 100% of the benefits of the ICE project would be retained for shareholders. *Id.* at 19:414-420.

Mr. Effron recommended that the Commission "should condition its approval of the Reorganization in the present case on the reduction to costs resulting from the in-service date of the ICE project (the cessation of the organizational readiness expenses and the 'hard benefits' in the form of other cost reductions) being properly credited to customers by means of a rider that would commence at the closing of the Transaction and would continue until the rates in the Gas Companies' next base rate case go into effect." AG Ex. 1.0 at 20:451-457.

In response to this proposal, JA witness Schott argued that by relying on information the Joint Applicants provided in JA Ex. 4.1 and in their data request responses related to the ICE project, AG witness Effron was "trying to use older information to call into question updated information." JA Ex. 9.0, at 22:476-480. But that criticism is simply untrue, the AG argues. The

AG points out that the so-called "older information" that Mr. Effron relied on is the data contained in the response to JA AG 3.05 Attach 01 CONFIDENTIAL (AG Ex. 1.5 Confidential). When asked to identify the differences between the "older information" and the "updated information", the Joint Applicants described one, and only one, change to what Mr. Schott characterizes as "older information." Specifically, the Joint Applicants stated that: "Subsequent to the compilation of data underlying JA AG 3.05 Attach 01 CONFIDENTIAL, the estimated ICE implementation date for the Gas Companies has moved from the second to the third quarter of 2015." *See* AG Ex. 1.7 (attached to Effron Direct).

The bottom line is that the delay in the estimated ICE implementation date by one quarter cannot possibly explain why the billing for the return on assets/depreciation on the ICE project would be moved forward from the beginning of 2016 to the beginning of 2015, as was assumed by the Gas Companies in the rate cases. Nor can the change in the implementation date possibly explain the other significant discrepancies in the treatment of ICE costs and benefits in the Gas Companies' rate cases, as described in Mr. Effron's Direct testimony.

Unless the Commission adopts Mr. Effron's proposed condition, PGL/NS customers will be paying $19.2 million per year for ICE costs for as long as the rates established in those cases are in effect, without getting the benefit of any of the offsetting system savings. The AG points out that the Joint Applicants have stated that they are "prepared to provide immediate benefits to customers and the Illinois communities the Gas Companies serve by making commitments that it would accept as conditions on the Commission's approval of the Reorganization." JA Ex. 1.0, at 15:331-334. Adoption of a mechanism that properly credits customers for the ICE savings is a reasonable condition for approval of the merger.

Staff argues in its Brief that AG witness Effron's proposal that any merger approval be conditioned on the JA's agreement to reflect an additional benefit to PGL/NS customers in rates based on new information in the record in this docket demonstrating that the Gas Companies will be experiencing significant savings post-merger related to the ICE project would constitute an unlawful rider. Staff IB at 43. The JA, on the other hand, characterized the proposal as unlawful retroactive ratemaking. JA IB at 41.

In reply, the AG argues that both interpretations of the proposal are incorrect. First, the AG points out, Mr. Effron's proposed condition is offered as an attempt to ensure that new information about the ICE project provided by the JA in this merger proceeding is reflected in customer rate going forward, not, as the JA suggest, to cure some past rate infraction. In no way does it seek any kind of retroactive adjustment of rates. It would not be implemented pursuant to any refund provision of the Act, but rather as a condition of the merger pursuant to Section 7-204(f) of the Act.

Second, the AG states that the Commission has specifically rejected the argument that rate adjustment proposals in the context of merger proceedings trigger single-issue and retroactive ratemaking concerns under Article IX principles. The Commission has stated:

> The fundamental requirement for a rate is that it must be just and reasonable, and a proposed rate change must also be just and reasonable. A rate must also be non-discriminatory, and, as discussed above, it cannot, per Section 9-230, reflect capital costs associated with non-regulated affiliates. Accordingly, a merger proposal that would likely render a rate unjust, unreasonable, discriminatory or infused with prohibited capital cost is adversely impacting that rate within the meaning of subsection 7-204(b)(7), irrespective of whether the rate will increase. Moreover, a merger proceeding involves a change of ownership, not ratemaking. Indeed, if ratemaking were allowed, the Commission would have to do the very thing the JA have decried throughout this proceeding - set rates without a full assessment of costs and revenues in a test year.

> Third, the prohibition against single-issue ratemaking is not, as JA claim, violated by focusing, in a reorganization proceeding, on fewer than all of the cost elements that the Commission considers when setting rates. Again, this is not a ratemaking case - a distinction the General Assembly certainly understood when it established different schemes for, respectively, reviewing merger requests and setting rates.

Nicor/AGL Resources Merger Order (Docket No. 11-0046) at 29-30. In that case, AG points out, the Commission rejected claims by AGL/Nicor that the "adverse rate impacts" prohibited by the statute cannot occur unless the "totality" of a merger, rather than a limited number of cost elements, will likely affect the utility's retail rates. Id. at 29. The Commission stated, "Absolutely nothing in the subsection states or implies that only the 'totality' of a proposed merger can have the precluded adverse impact. Subsection (b)(7) bars 'any' likely adverse rate impact, of whatever cause associated with reorganization. Indeed, the Commission cannot perceive what would constitute the 'totality' of merger, why the legislature would not protect retail customers from adverse rate impacts resulting from less than a 'totality,' or why resources should be expended debating or implementing a 'totality' standard." *Id.*

In the instant case, according to the AG, the evidence makes clear that unless action is taken under Section 7-204(f), ratepayers will be adversely impacted by rates that reflect all of the costs but none of the savings associated with the ICE project. Moreover, contrary to Staff's unlawful rider argument, the proposal by Mr. Effron is not intended to be a permanent rider mechanism. Rather it is intended to provide the benefit that the Joint Applicants' discovery responses indicate will occur in 2015 and beyond. If the Commission is uncomfortable in recognizing this benefit through a rider refund mechanism, it should calculate the value of the ICE-related benefit for the period of any rate freeze and provide a one-time refund to PGL/NS customers at the close of the merger. The evidence in this case shows that if there is no adjustment to the ICE costs forecasted by the Gas Companies in those cases and the "hard benefits" commence with the in-service date of the ICE project, as the Joint Applicants assert will occur, the Gas Companies will be recovering $19.2 million annually in non-existent expenses when the ICE project goes into service. AG Ex. 1.0 (Effron Direct) at 18-19:409-414. In effect, during the term of the proposed rate freeze, the customers would be charged for all of the annual costs of the ICE project, while 100% of the benefits of the ICE project would be retained for shareholders. Id. at 19:414-420.

For all of these reasons, the AG states that Mr. Effron's proposal (or a modification of that proposal that captures this revenue difference) should be adopted as a condition of any Commission merger approval, pursuant to Section 7-204(f).

vi. AG witness Effron's proposal to reflect the difference between employee numbers projections currently reflected in PGL/NS rate and the JA's "floor" employee number commitment should be adopted as a merger condition.

In order to provide any value to the WEC employee number commitment, Mr. Effron recommended that the Commission condition merger approval on any savings due to the difference between the headcounts for the Test Year reflected in the revenue requirements presented by the Gas Companies in Docket Nos. 14-0224/14-0225 (cons.) and the Joint Applicants' employee headcount commitment in the present case being properly credited to customers. One option recommended by the AG would be to credit to customers the savings associated with a decreased employee complement post-merger, as compared to the FTE numbers PGL and NS forecasted in the rate case – a number that is reflected in current customer rates. Mr. Effron proposed that the differential in expense associated with these conflicting numbers be returned to PGL/NS customers by means of a rider that would commence at the closing of the Transaction and would continue until the rates in the Gas Companies' next base rate case go into effect. AG Ex. 1.0 at 20:437-444. The rider would be no different than any other merger commitment; it would exist because the JA had agreed to implement it to ensure that customers were not financially harmed by the merger, consistent with Sections 7-204(b)(1) and (7) of the Act.

The AG notes that the Joint Applicants' characterization of the minimum employee headcount commitment as a benefit to customers in the present case is inconsistent with the test-year employee headcounts presented by the Gas Companies in the rate cases as being necessary to provide safe and reliable service. The AG argues that Mr. Effron's rider credit proposal is an effort to give some substance to the Joint Applicants' minimum employee headcount commitment, on a *forward looking* basis. The proposal would ensure the public interest by resolving the inconsistency that PGL and NS created by forecasting higher FTE numbers in the rate case (thereby maximizing revenues) and the JA's commitment in this docket to a lower combined FTE number post-merger – a number that the JA admit is lower than the FTE amount that "will be needed to provide adequate, reliable, efficient, safe, and least-cost service in 2015 and 2016." JA Ex. 6.0 at 26:681-684.

In their Reply Brief, Staff argued that it, like Mr. Effron, is troubled by the fact that the number of employees that the JA have committed they will retain after the close of any reorganization is significantly lower than the level of employees the Gas Companies forecasted and the Commission approved in the just-completed 2014 PGL/NS rate case. Staff points out the same flaws in the JA's commitment to retain a total of 1,953 employees for PGL, NS and Integrys Business Support two years post-merger that the People identified in their Initial Brief: (1) the commitment, while based on assumed Full-Time Equivalent ("FTE") numbers for each Gas Company and Integrys Business Support, is made in the aggregate, not by company; (2)

there is no description of how this commitment breaks down between administrative support and front line operational employees; (3) the 1,953 FTE commitment breaks down to 1,294 FTEs for Peoples Gas and 166 FTEs for North Shore; and (4) in the recently completed PGL/NS rate case, Docket Nos. 14-0224/0225 (cons.), Peoples Gas and North Shore forecasted 1,356 and 178 FTEs, respectively, for the 2015 test year, which presumably represent the level of FTEs needed to provide adequate, reliable, efficient, safe, and least-cost service in 2015 and 2016. Staff IB at 11-16. Staff seeks to require the JA to retain the number of employees that are currently represented in rates, i.e. the numbers forecasted for the 2015 test year in Docket No. 14-0224/-0225. Staff Ex. 9.0 at 21:520-522.

In response to that request, the JA proposed an alternative commitment to retain this higher number of employees for at least two years after the close of the requested reorganization. The AG states that the Commission should implement that condition should it approve the merger. That being said, if numbers drop below that level, in order to provide any value to the WEC employee number commitment, Mr. Effron's recommendation that the Commission condition merger approval on the proper crediting to ratepayers of any savings due to the difference between the headcounts for the Test Year reflected in the revenue requirements presented by the Gas Companies in Docket Nos. 14-0224/14-0225 (cons.) and the Joint Applicants' employee headcount commitment in the present case should be adopted.
The rider would be no different than any other merger commitment; it would exist because the JA had agreed to implement it to ensure that customers were not financially harmed by the merger, consistent with Section 7-204(b)(1) and (7) of the Act.

The AG pointed out Mr. Effron's rider credit proposal is an effort to give some substance to the Joint Applicants' minimum employee headcount commitment, on a *forward looking* basis, contrary to the JA's claim that to do so would constitute unlawful retroactive ratemaking. JA IB at 40-41. Again, Section 7-204(f) of the Act provides the Commission with the ability to impose conditions on a merger approval that it believes are necessary to protect the public interest. Stating one thing in a rate case (that the Company will need X number of employees, which will be reflected in customer rates) and then agreeing to maintain a lower number of employees as an alleged benefit of the proposed merger is hardly a win for ratepayers, and arguably diminishes the safety, reliability and least cost nature of utility service, as prohibited under Section 7-204(b)(1) of the Act. It represents an effort to ensure that the number of employees that "will be needed to provide adequate, reliable, efficient, safe, and least-cost service in 2015 and 2016" (JA Ex. 6.0 at 26:681-684) is actually reflected in customer rates. The AG states that it should be adopted by the Commission, along with the JA's alternative FTE commitment.

vii. The Commission should condition the merger on exclusion of all transaction costs, including any severance packages.

The AG argues that while the Joint Applicants state that they will not seek recovery of costs incurred to accomplish the reorganization, including transaction, change in control, financing and "legal/other professional" costs[30], City/CUB witness Gorman notes that it is not clear whether all costs associated with the reorganization transaction will not be recovered from ratepayers. He recommended that the Commission condition any merger approval by specifically prohibiting recovery in rates of any executive, Board of Director or senior employee severance costs or early termination fees, i.e. severance packages. City/CUB Ex. 4.0 at 11:255-262. To be clear, Mr. Gorman explained costs incurred in order to produce savings should be permitted in rate recovery up to the level of savings created. City/CUB Ex. 8.0 (Gorman

[30] JA Ex. 2.0REV at 11:236-243.

Rebuttal) at 5:94-96. He noted that if transition costs are included in a future rate case test year, then the Joint Applicants have the burden of proving that there are savings within the test year and over the life of the project that fully offset the level of transition costs. *Id.* at 6:113-116.

This condition should be attached to any Commission merger approval as well, according to the AG.

B. Commission Analysis and Conclusion Regarding Section 7-204(f)

As we noted in the portions of this Order that address Section 7-204(b)(1) and (b)(7) above, unless conditions are attached to the proposed merger, we cannot conclude that the merger would not diminish the utility's ability "to provide adequate, reliable, efficient, safe, and least-cost public utility service" (220 ILCS 5/7-204(b)(1)) and that the proposed transaction "is not likely to result in any adverse rate impacts on retail customers." 220 ILCS 7-204(b)(7). In addition, we are mindful of the AG's statement in their Initial Brief that the Commission cannot protect the interests of the utilities and their customers, as it is required to do under Sections 7-204(b) and (f) of the Act, if it is investigating allegations of wrongdoing involving WEC and other members of the Joint Applicants in Docket No. 15-0186 but simultaneously moving ahead with a decision as to whether WEC should be permitted to acquire the Gas Companies in this docket. Moving forward to approve a merger under these circumstances is contrary to the ICC's obligation to protect the interests of utility customers is a difficult enterprise. 220 ILCS 5/ 7-204(b),(f). Without having completed its investigation into the alleged wrongdoing, the Commission is concerned as to whether the transaction will prolong or exacerbate dysfunction in PGL's AMRP. Indeed, the Commission has already asserted a connection between the merger and the investigation. Docket No. 15-0186, Corrected Initiating Order at 1.

Notwithstanding these procedural and evidentiary barriers to satisfying Section 7-204 requirements, the Commission believes the addition of several minimum conditions should be attached to the proposed reorganization that we hope will ameliorate our significant concerns about WEC's assuming the role of corporate parent over the Gas Companies. As a starting point for the Commission's 7-204(f) analysis, we note that the record evidence shows that the list of commitments that the Joint Applicants have included as JA Ex. 15.1 REV as a condition of the merger are woefully insufficient to protect ratepayers and the public interest in general, as discussed above.

Accordingly, we hereby adopt the conditions recommend by the AG to help ensure that the merger will not diminish the Gas Companies' ability "to provide adequate, reliable, efficient, safe, and least-cost public utility service" (220 ILCS 5/7-204(b)(1)) and that the proposed transaction "is not likely to result in any adverse rate impacts on retail customers." 220 ILCS 7-204(b)(7). In addition, the protection of the public interest pursuant to Section 7-204(f) demands that the Joint Applicants commit to the conditions that are attached as Appendix A.

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Respectfully submitted,

PEOPLE OF THE STATE OF ILLINOIS
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